The Indonesian Quarterly

Fourth Quarter 2009 Vol. 37 No. 4

Indonesia and the Global Financial Crisis

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Centre for Strategic and International Studies

The Indonesian Quarterly
Fourth Quarter 2009
Vol. 37, No. 4

The Indonesian Quarterly is a journal of policy oriented studies published by the Centre for Strategic and International Studies (CSIS), The Jakarta Post Building 3rd Floor, Jalan Palmerah Barat No. 142-143, Jakarta 10270, Indonesia. It is a medium for research findings, evaluations and views of scholars, statesmen and thinkers on the Indonesian situation and its problems. It is also a medium for Indonesian views on regional and global problems. The opinions expressed in *The Indonesian Quarterly* are those of their authors and do not necessarily reflect the opinion of the CSIS.

The Logo

To better represent the underlying ideas that gave birth to CSIS in 1971, the Centre uses as of 1989 the logo that figures on the front cover of this journal. The original, in bronze, was designed by Indonesia's renowned sculptor G. Sidharta and comprises a disc with an engraving of the globe, which serves as a backdrop to a youth with an open book on a cloth draped across his lap, his left hand pointing into the book, and his right raised upwards. All these elements combine to project the Centre's nature as an institution, where people think, learn and share their knowledge. Mankind is their concern and the world their horizon. The undressed torso symbolises open-mindedness and the absence of prejudice in the attitude of the scholars who work with the Centre, just as it is with scholars everywhere. The inscription reads "Nalar Ajar Terusan Budi", in the Javanese language, conveys the Centre's belief that "to think and to share knowledge are the natural consequences of an enlightened mind." It is a surya sengkala that is chandra sengkala - a Javanese traditional way to symbolise a commemorable year in the lunar calendar, adapted to the solar calendar system. It uses words that express the perceived meaning of the commemorated year while marking the year at the same time, with each word having a numerical value. Thus, the inscription, in reverse order, represents the year CSIS was established: 1971.

SIT 01381/SK/Dirjen PG/SIT/72

ISSN 0304-2170

The Indonesian Quarterly

Fourth Quarter Vol. 37 No. 4, 2009

Indonesia-and the Global Financial Crisis

Economic Reform and Institutions in Indonesia

Three main conclusions emerge from the authors' examination of the Indonesian experience of the political economy of public policy and reform. First, there were differences related to specific interplay of ideas, institutions, interests and political and bureaucratic actors in each of the case studies. Second, in all cases of reform discussed in the article, it was Presidential support or lack of support for reform that played a decisive role. In particular, reforms involving complex distributive outcomes require strong support from the President. Third, given the right preconditions, reform can be undertaken more quickly and can be more comprehensive in a more autocratic rather than a more democratic system of government. Especially in a new democratic system, where parties appeal on the basis of broad and often shifting principles, rather than clearly defined policies, interest groups are often able to mobilise demonstrations of support through the mass media and thus convince political actors to back their cause.

The article examines the importance of domestic institutions on three areas: the success of decentralization, improving welfare, and contributions to regional as well as global institutions. Direct local elections have given rise to local capture. Without a strong legal institution at the district level, decentralization could have an adverse effect. Stability in macroeconomic sector has not been followed by an improvement in poverty, inequality, and unemployment. Reforming institutions at the microeconomic level are necessary. Transparency of the Central Bank is needed for regional and global coordination, which is shown to rely much on political fundamentals. Increased quality of information between the government and the public might also help to solve regional and global issues, such as regional infrastructures and carbon trading.

Gender and Regional Trade Liberalization

There is little doubt that trade liberalization has had a profound effect on the well-being of women in Southeast Asia. Not all of these impacts are negative, however. Indeed, the opening up of the region's economies, at both national and regional levels, has brought about opportunities in the form of new employment, which may allow them to access higher incomes and improve

their status in the society. Given their increasing role in the economies of Southeast Asia, however, women are often the major victims of economic openness. Poor women, in particular, remain vulnerable to economic policy changes that occur in the region.

This paper analyzes the gender-sensitivity of selected trade liberalization initiatives pursued by the countries of Southeast Asia. It primarily argues that trade policies and agreements pursued by both ASEAN and its member countries are far from being gender sensitive. Given the prevalent view among trade policy-makers that trade is gender-neutral, the absence of substantive considerations of the implications of economic opening towards the well-being of women risks undermining the sustainable livelihood of this dynamic group of society.

Review of Developments

Indonesia's economy showed uncertainties in the mid of 2008. These uncertainties persisted in the first semester of 2009 as the global financial crisis still continues to threaten the national economy aggravated by the slump in other economies around the world. However, Indonesia's government was quick to respond by combining both monetary and fiscal policy instruments in order to at least minimize global crisis impacts on Indonesia's election year of 2009. Swift action in the handling of the rapid depreciation of the Rupiah since August 2008 had helped the government successfully manage to avoid the sudden meltdown of 1998.

In recent months, developments in Indonesia's geostrategic landscape, especially in the Asia Pacific region, seem to follow existing trends in the past few years. The main trends in this regard are the continued rise in overall defense spending, the growing sophistication of naval and air force, and the growing self-reliance of regional defense industries. Indonesia is way behind in terms of force development. Investments in R&D, as well as innovative procurement strategies geared to strengthen domestic defense industry with the long term vision of self-sufficiency, have all stood behind the growing sophistication of regional militaries. Indonesia's key neighbor, especially Malaysia and Singapore, have also increased their naval and air power projection capabilities significantly—which further widens the regional gap between the three countries.

THE IMPACT OF THE GLOBAL CRISIS ON INDONESIA

Cyrillus Harinowo

It has been over one year now that the global crisis that started in the United States has evolved. A crisis of a colossal magnitude created tremors all over the world that required concerted efforts in putting them down. Currently signs of recovery have been evident in several places. However, we need to be cautious in order not to be misled by a false hope.

Since the crisis impacted the global economy, what was the kind of impact that the global crisis had on Indonesia? It is always interesting to see from the rear view mirror, because we can always learn from hind-sight. In this respect, one year has been sufficiently long for us to draw some lessons. However, before we go into the details with what happened in Indonesia, it might be useful to review how the crisis started to evolve.

HOW THE CRISIS EVOLVED

The global imbalances that originated from the United States have been going on for many years. While the balance of payments deficit has lasted almost "forever", yet the present US government's budget deficit was a new phenomenon. It was totally the reverse of the surplus that was previously generated by the Clinton administration. Then, the twin deficit had been predicted as the potential source of global

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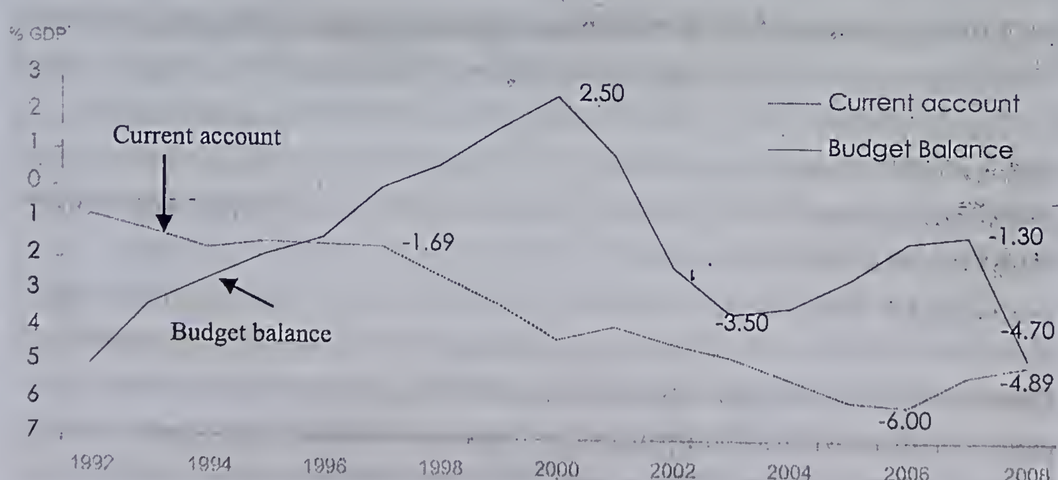
economic disruption. However, the US current economic crisis was apparently driven by another source, the greed in its financial sector.

It has been over a year since the US Financial System entered a new stage after the Treasury and the Fed proposed a US 700 billion bail-out of their financial system. This amount, around 5% of GDP, seems big. However, looking at the size of the problem and the potential fall-outs, this amount seems to be reasonable when viewed from that time's perspective. Now we can conclude that the bail-out was a clever idea in preventing a larger financial crisis from occurring in the US.

The breath of the bail-out was not entirely clear when it was decided, but by now we can see a number of things that have come to the surface. However, coming to a rescue of the financial system at that stage can be considered a preemptive move before things become out of hand. This was also the reason why the amount, USD700 billion, was considered adequate to prop up the confidence to the financial system. The amount itself was a show of how serious the US Government in tackling the situation. If the authorities were late in making the move, the financial system might experience runs of their banks (like what had been experienced by the Northern Rock Bank in UK) that will change the current situation into entirely different game. If that happened, the total bill will be much larger than what had been proposed.

Chart 1. The Evolution of the Twin Deficit



The problem in the US Financial System was indeed a colossal one. Until then none of the commercial banks have been bailed-out by the Government, although many banks had been closed or bailed out by the FDIC (Federal Deposit Insurance Corporation). As we all know, Bear Sterns, Merrill Lynch and AIG were the ones receiving life-lines. Fannie Mae and Freddie Mac were also rescued. This was really unprecedented because the prevailing wisdom was that the bail out only applied to the commercial banks. However, the prompt actions by the US Government were also driven by concerns over the integrity of the banking systems. Through various inter-bank and capital market transactions, letting these institutions go would trigger a domino effect in the banking system. Maybe partly because of that the two giant investment banks, Goldman Sachs and Morgan Stanley, were finally also given up as the two remaining investment bank giants to become "bank holding companies" to gain permanent access to the Federal Reserve's funds.

The financial crisis was initially driven by a crisis in the sub-prime mortgage. The housing boom (or bubbles) in the last few years created an atmosphere for the financial system to expand very rapidly, including to non-creditworthy customers. In the US system, these mortgages were then bundled, repackaged, and sold to the capital market in the form of Mortgage Backed Securities (MBS) and its variants such as CDO (Collateralized Debt Obligation).

Therefore, while the initiators of the mortgages were commercial banks, savings-loans companies and mortgage companies, the investment banks were involved through its portfolios in the MBS and CDO that they purchased from the capital market. Fannie Mae and Freddie Mac were also actively playing a role as a bridge in securitizing these loans. Having this role, often times the two institutions also had to take some securities on their portfolio. All these things could smoothly happen since these assets were rated triple A by agencies such as Standard and Poor and Moody's.

If the problem was limited to that issue, things were still manageable. Both MBS and CDO were portfolios with underlying assets. In that case, any problems with the underlying assets, which were mortgages, still could be deciphered by the authorities. However, things became blurred once other factors finally came to surface in the name

of CDS (Credit Default Swap). This was a new "animal" in this complex game.

CDS is a new instrument invented in the 1990s to provide insurance to the financial system when their bonds, loans or other assets are in default. The seller of this instrument provides a guarantee if the bond or other asset is in default. For this purpose, the buyer of the instrument has to pay annually for the life of the contract period, say for five years. For this purpose, in return, the sellers have to set aside certain amount of assets as collateral. If the transaction follows this mechanism, things may still go on very smoothly because the risk is measurable. In fact, the transaction was initiated because the buying party wants to mitigate its risk.

In practice, however, many of the sellers, some of which are hedged fund companies, did not abide by this rule. As an example, a small hedged fund company in the US was willing to have such a transaction with one large Swiss bank without bowing to this collateral requirement. This posed a serious counter-party risk to the Swiss bank that finally cancelled the contract. In quiet time, like what happened in the US for many years, things went on smoothly. But once the water gets rough, the system is cracking.

What made these things more serious were excesses in this kind of transaction. Since there is no tracking mechanism, therefore the transaction can be done repeatedly. Sometimes, a transaction to insure Bond A held by Institution X was done more than five times by the sellers with other parties without any presence of the bond. Therefore, if things go sour, it will be difficult to track down the amount defaulted. Legal wrangling through litigations and counter litigations will take place just to resolve one transaction. Things may become badly muddled..

It was this CDS that became the ultimate monster of the recent financial crisis. Since there was no transparent way in disclosing this instrument, people predicted that the amount involved could be as high as USD 42 trillion, more than three times of the US GDP. Lehman Brothers were the victim of this instrument. The same also happened to other institutions that finally were bailed out.

In a crisis of this scale, building confidence became a very critical part of the game. Whatever happened with the market reactions, action by the US Government deserves praise. While discussion was still

on going on the modalities of the rescue, people could hope that their money in the banks was safe. People had witnessed that if something happened with their banks, either FDIC (such as what happened with many banks), or the Treasury and the Fed would take prompt actions to resolve the problem.

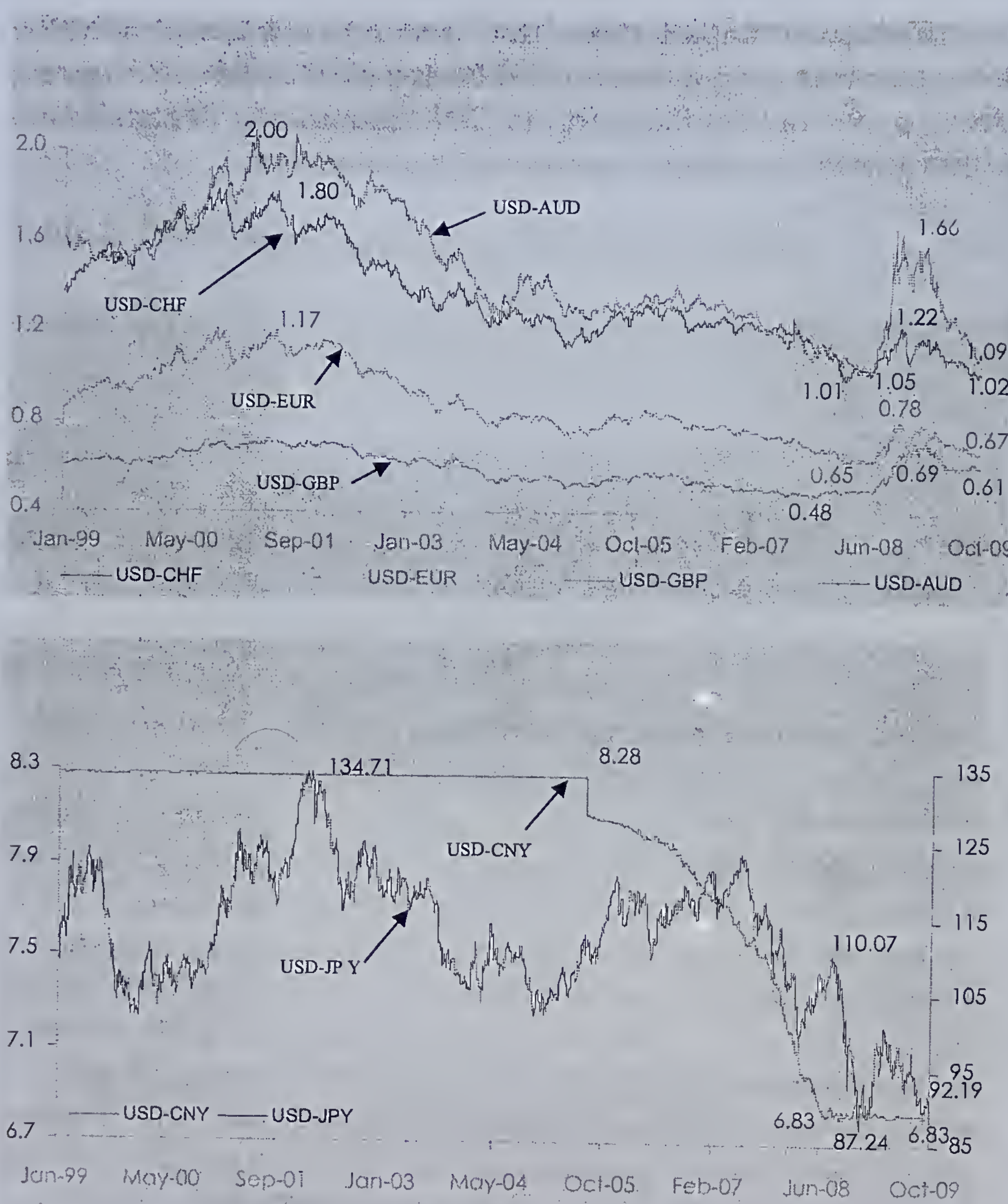
The crisis of the US financial sector could be seen as the first wave of the economic tsunami. This was followed by the contraction of the economy. In the US, in the run up toward the big tsunami, the economy was already seriously beaten. The economic growth had stumbled and was followed by a major contraction. The technical recession, defined as two quarters of economic contraction, started in 2007 and continued until this day. This recession formed the second wave of the tsunami.

TRANSMISSION CHANNELS OF THE US CRISIS TO THE GLOBAL ECONOMY

It was widely believed that when the US sneezes, other countries will catch cold. There are two major channels that transmit the US economic disease to other countries, capital flows and through the trade.

At the peak of the financial crisis, many US companies suffered a liquidity squeeze that has to be quickly solved. As a result, many companies, including banks and investment funds, withdrew their investment from all over the world and brought them back to the United States. This process, called "de-leveraging", finally led to a massive weakening of the value of other currencies vis-à-vis the US Dollar. It is only after a while that this process started to reverse again.

Chart 2. Exchange Rates

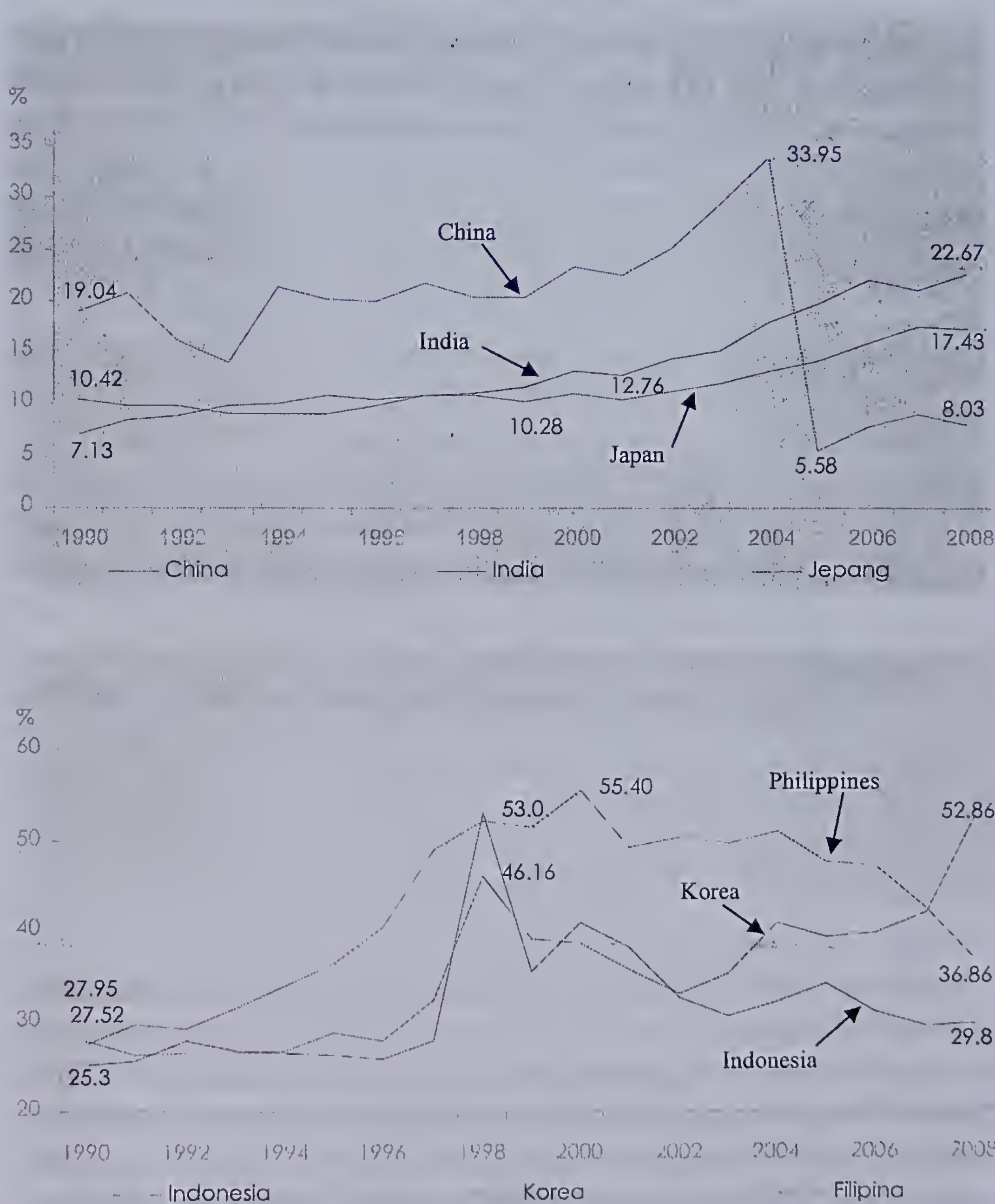


On the second channel, the contraction of the US economy depressed US demand for import products. The US economy is indeed very big. The total GDP generated by the superpower is around USD14 trillion, 28 times of the Indonesian economy. An economy with such magnitude sucks various products from all over the world to meet the needs of their industries as well as their people. Therefore, when there

is a contraction on the economy, the exports of other countries to that superpower will be heavily affected.

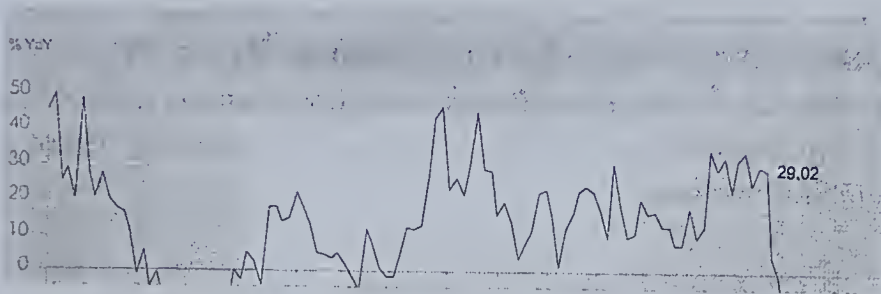
The relative impact varies from country to country. From the Asian countries perspective, the relative impact is determined, among others, by the ratio of the export to GDP. Countries with higher ratio will be affected more than countries with a lower ratio.

Chart 3. The Ratio of Exports to GDP



The drop in exports from various countries resulted in the decline of their economic growth. Depending on their export ratio, many countries started to experience very low growth. After a while, such low growth turned to become major contractions for major countries as well as many Asian countries.

Table 1. Economic Growth in Selected Countries



THE IMPACT OF THE GLOBAL CRISIS ON THE INDONESIAN ECONOMY

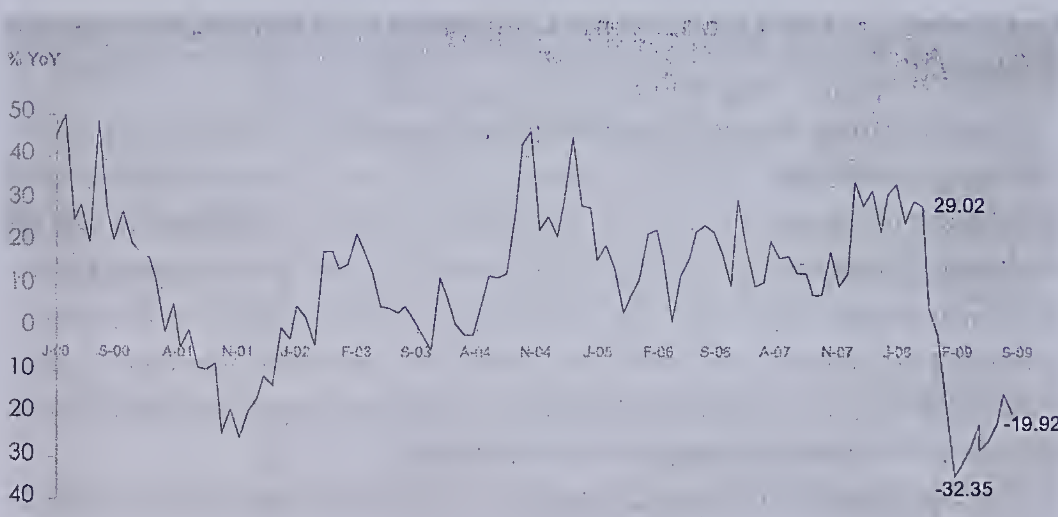
At one time, questions arose whether Asian countries would be affected by the crisis. These questions arose because initially many Asian countries were still able to weather the crisis. Therefore, an issue of an "economic decoupling" became one of the interesting topics of the discussions. However, by the fourth quarter of 2009, it became evident that many Asian countries were also seriously affected. Singapore, Thailand and Malaysia started to feel the pinch and fell into recession. What then happened to Indonesia?

The Indonesian financial sector was the first to be seriously impacted by the crisis. The deleveraging process led to a sharp weakening of the Rupiah that depressed the sentiment. At the same time, there was a serious liquidity squeeze due to the deleveraging process. Later, it was discovered that a major cause of such liquidity squeeze includes the contraction of the Government sector. The Government piled up a lot of cash in Bank Indonesia since the expenditures did not match with the revenues. The closure of the Indover Bank, a subsidiary of the Central Bank of Indonesia, coupled with the serious problem on the massive bail-out of Bank Century, also had made the financial sector shaking. Fortunately the Central Bank and the Government moved

fast. The Central Bank loosened the liquidity by significantly lowering the reserve ratio. In fact, it was done twice in order to stabilize the liquidity in the banking system. At the same time, the Indonesian Government also announced a major fiscal stimulus. With that policy, the Indonesian financial sector was prevented from melting down.

The Indonesian export sector also suffered significantly from the global downturn. From the peak performance of monthly export of around USD12.5 billion, Indonesian exports saw a serious drop to only around less than USD10 billion. For a number of commodities, especially CPO, the drop in demand led to a downfall of its price that affected the welfare of the estates and the farmers. Fortunately, the price started to swing up again, creating better sentiments among the commodities regions in Indonesia.

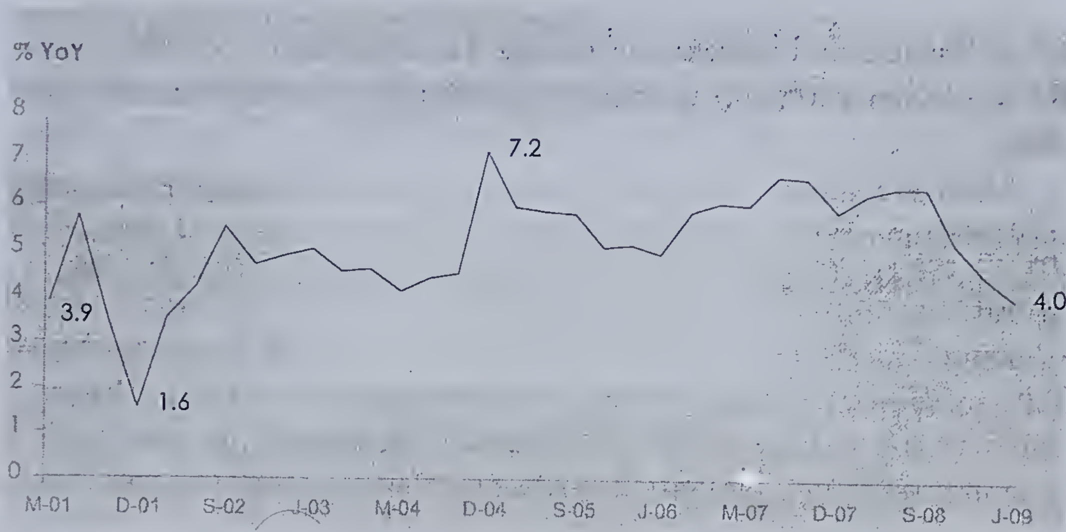
Chart 4. Export Performance



Understandably, many economists were skeptical about the Indonesian economic performance. Yet, there were conflicting evidences from various companies that their sales performance remained growing. Surprisingly, the consumer products, including electronic sector, still experience a growing demand. Moreover, rice productions as well as other agricultural products turned out to be very promising too. Thus, it was a real relieve to know that the economic performance in the first quarter of 2009 still experience a positive growth of around

4.5%. In nominal term, the growth rate was still respectable at the rate of 16.9%. Such performance was repeated again in the second quarter of 2009. The GDP was growing at the rate of 4.1%. Nominally, it was growing at the rate of 10.9%. Therefore, Indonesian economy stood to be resilient in weathering the crisis.

Chart 5. Quarterly GDP Growth



From what happened in the past few quarters, three big countries—i.e., China, India and Indonesia—have proved themselves to have successfully avoided the negative growth.. This performance immediately attracted the global spotlight. Justifiably, it was the demographic factor that had saved Indonesia from the global crisis. The same also true for the other two countries—China and India—as they also represent countries with big population. Thus, the domestic demand generated by the population could help offset the significant drop in exports at times of economic crisis. The balanced economy seemed to hedge between the external demand and the domestic demand.

Indonesia is currently preparing itself for 2010. It was extensively believed that the year 2010 will bring better prosperity to the Indonesian economy.

CONCLUSION

The global economic crisis has swept countries all over the world in the past few quarters, with recessions taking place in the advanced as

well as many emerging countries. However, there were three countries that could stand the heat and emerged with positive growth, namely China, India, and Indonesia.

The Indonesian economy was initially also affected by the global crisis through the deleveraging process of the foreign portfolio investment as well as the negative impact on the export sector. Nonetheless, the Central Bank and the Indonesian Government reacted swiftly by loosening the liquidity crunch and launching a major fiscal stimulus, which turned out be effectively curing. The steps have successfully stabilized the market; and gradually the economy was back on the right track.

In the mean time, the government of Indonesia has been preparing itself for the next five years term with a lot of anticipation. Therefore, it is widely expected that the next five years will be a promising period.

IN THE MIDST OF GLOBAL FINANCIAL SLOWDOWN: THE INDONESIAN EXPERIENCE*

Reza Siregar and Willeam Wiranto

INTRODUCTION

Having been among the most severely hit economy by the Asian financial crisis of 1997-1998, Indonesia, based on many measures, weathered the global slump of 2008-2009 remarkably well. The country maintained the third-highest gross domestic product (GDP) growth in the Group of Twenty economies (G-20) and the major Asia Pacific economies—slower only to China and India, averaging higher than 4% quarterly during the first half of 2009 (Table 1).

Table 1: Growth Performance of Selected Countries

	2009 GDP Growth Projection	
Country	Initial	Revised
Malaysia	4.8	0.2
Thailand	4.5	2
Australia	2.2	1.7

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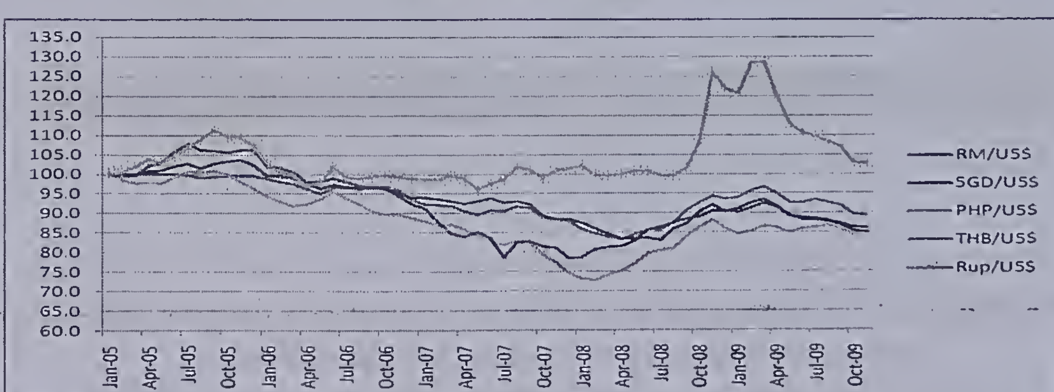
*/ The opinions expressed in this study are of the authors alone, and do not necessarily represent the SEACEN Centre.

Indonesia*	6	4.5
USA	0.1	-0.8
UK	-0.1	-1.3
Singapore	3.5	-5
Japan	0.5	-0.2
South Korea	3.5	2.5
India	6.9	6
China	9.3	8

Source: CEIC Database

The country's large domestic market and its relatively low dependency on external trade fuelled the country's economic growth amidst global economic recession. Robust growth in private consumption, underpinned by both moderate inflationary pressure and a surge in election-related spending, contributed close to 60% of GDP during the first half of 2009. Annualized headline inflation bottomed in July 2009 at around 2.7% from over 11% at the end of 2008. However, with the return of rising commodity prices since the second half of 2009, especially with the crude oil price in the global market, a stronger inflationary pressure was recorded in Q-3 of 2009.

Figure 1: Bilateral Nominal Exchange Rate against the US dollar (Monthly average and January 2005=100)



Source: The University of British Columbia, Sauder School of Business, Pacific Exchange Rate
Service Database (http://fx.sauder.ubc.ca/data.html

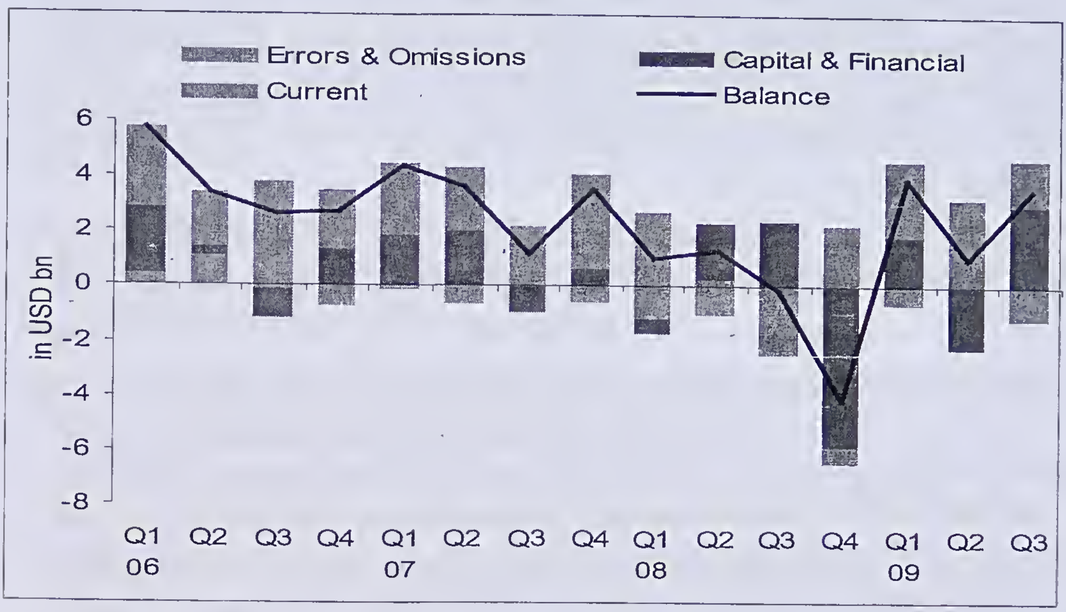
Following three consecutive quarters of current account deficits in 2008, the country reported a surplus in average of USD3.0 billion during the first two quarters of 2009. The strength of the trade surplus mitigated the impacts of the deterioration of the capital and financial account, and improved the overall balance of payment position, contributing to the rise in the foreign exchange reserve from USD 51.6 billion at the end of 2008 to USD57.4 billion in July 2009. The relative vigour of the Indonesian economy, and the success of parliamentary and presidential elections, particularly the successful reelection of President Susilo Bambang Yudhoyono to his second term, brought about a healthy return of investor confidence. Between January and August 2009, the Indonesia stock-market index has gained 95% in the USD term, albeit still below its 2008 peak. Accordingly, the return of the capital inflow triggered an appreciation trend in the local currency. Rupiah strengthened against most major currencies, in particular against the US dollar. The Indonesian rupiah (IDR) appreciated to around 1USD to IDR9400 in early October 2009 from its weakest point at 1USD to IDR12200 in November 2008 (Figure 1).

The objective of our study is to debate and review a number of factors frequently underlined as the foundations to the strength and resilient economic growth of the country in recent years. Next section examines closely the strength of the balance of payment of the country. In addition to the rapid return of portfolio investment, the role of primary commodities and the diverse export destinations mitigated the impacts of the global financial crisis on the country's balance of payment position. Subsequently, we assess the country's management of macroeconomic policies, especially monetary and fiscal policies, and discuss the overall effectiveness of these policy measures. Going forward, the country must rely less on its domestic consumption, and more on investment, especially the direct investment. To attract future investment, both domestic and foreign, the country must first address the dire stage of its infrastructure bottlenecks. The following section explores the regretful stage of the country's infrastructure. Brief concluding section ends the paper.

BALANCE OF PAYMENT: PLEASANT SUIDRRISE AND HEIGHTENED EXPECTATION

Indonesia's balance of payments situation has improved markedly, registering net surpluses for the first three quarters of 2009. This is a welcome contrast from the worrying trajectory experienced by the overall balance during the global turmoil, which accelerated in the second half of 2008 after the collapse of Lehman Brothers. From a net deficit of USD4.2 billion in the fourth quarter of 2008, the country's external balance has improved to a quarterly average surplus of USD2.9 billion in 2009 (Figure 2).

Figure 2: Balance of Payments

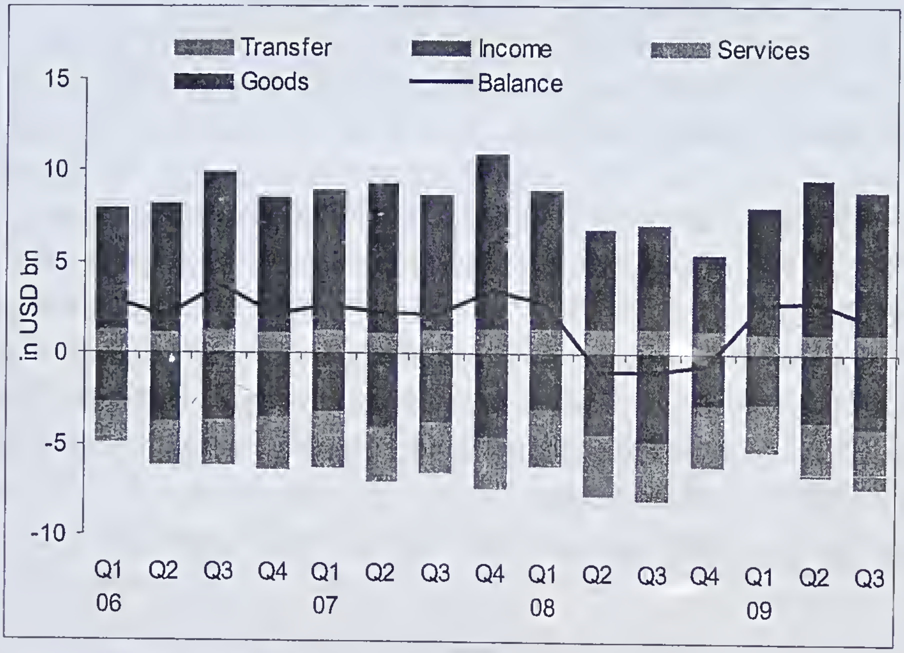


Source: CEIC Asia-Database

Looking at the compositions of the country's balance of payment, the current account balance has stayed at a comfortably positive level in 2009, adding stability to the overall external balance surplus for the country. Considering that the country had been running a current account deficit from the second to the fourth quarter of 2008, this development is especially heartening (Figure 3). While the relative stability in the level of worker remittances inflows and profit repatriations of foreign firms have helped to sustain the current account levels, the

healthy overall surplus in recent quarters has been ultimately due to a strong performance in goods and services balance. Compared to the lackluster balance in the fourth quarter of 2008, which dipped below USD 1billion, the goods and services balance has been healthy this year, with an average of USD4.8 billion a quarter year-to-date. The latest number in the third quarter of 2009 at USD4.6 billion adds to the confidence that the trade balance will continue to be helpful to the country's external payments conditions.

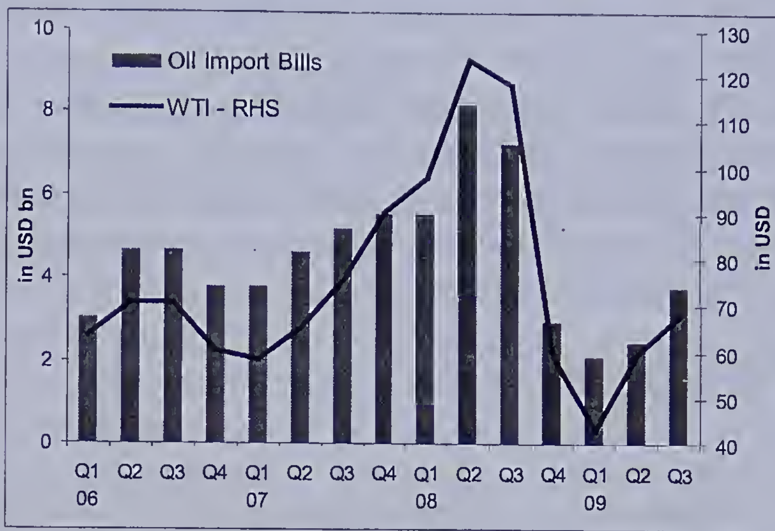
Figure 3: Current Accounts



Source: CEIC Asia Database

A bottoming in exports coupled with a collapse in imports resulted in a favourable goods and services balance. The overall trade balance has stayed positive throughout this year, due in part to the fact that the country's import bills for oil have come down dramatically alongside the drop in global oil prices (Figure 4). The prevalent gap between the recovery in exports and imports can be further explained by the fact that Indonesia is primarily a commodity-heavy raw materials exporter.

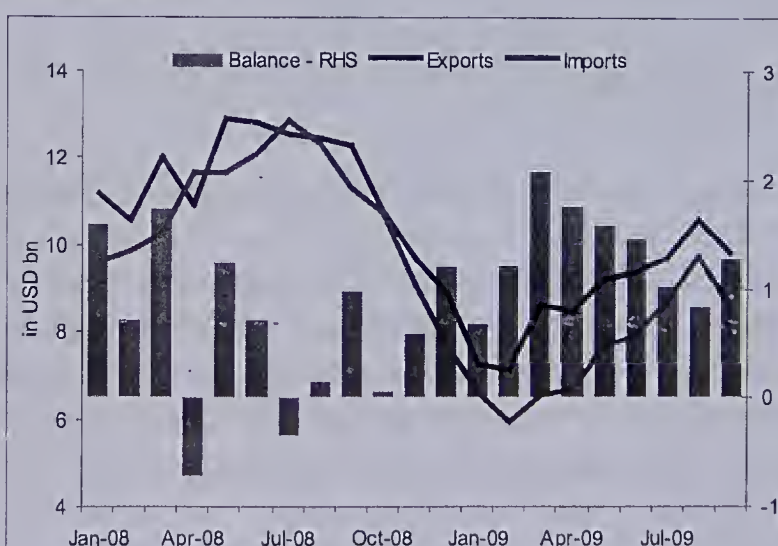
Figure 4: Oil Import Bills and Global Oil Price



Source: CEIC Asia Database

Manufactured goods constitute only 16% of Indonesia's total exports since 2006. In comparison, up to 53% and 44% of the total exports of Singapore and Malaysia respectively come from manufacturing of electronics alone. Therefore, unlike its neighbors which are more manufacturing-dependent and focus on the processing of imported intermediate goods for exports, Indonesia's imports do not necessarily lead its export numbers (Figure 5).

Figure 5: Trade Balance



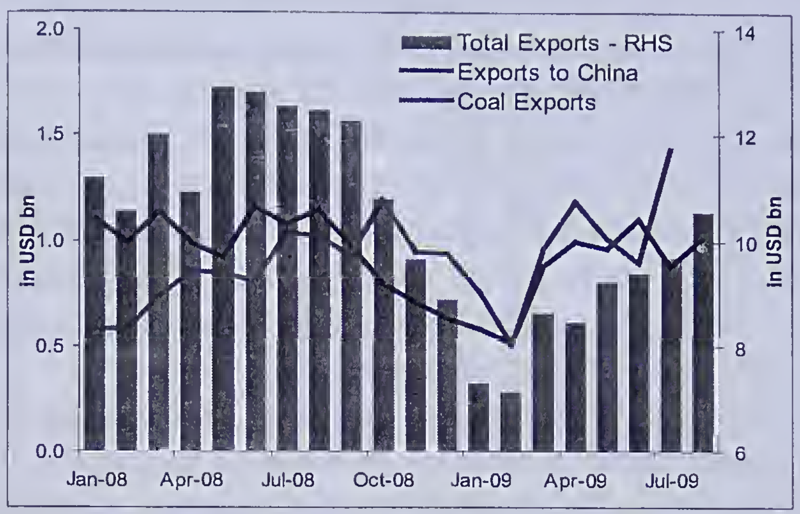
Source: CEIC Asia Database

In addition, the destinations of the Indonesian exports are relatively diverse. The big traditional export destinations such as the United States and the European markets, countries severely affected by the recent crisis, absorbed only around 25% of Indonesian exports during the first three quarters of 2009. While the Southeast Asian neighbours consumed around 22% of the country's exports for the same period. In 2009, Indonesia has in fact exported more to China and India, than to the United States. A similar general picture can be drawn from the import number. Hence, the Indonesian trade sector arguably faced more of second-round effects of the recent global slowdowns.

The improvement in Indonesia's exports also appears to have been driven primarily by a recovery in commodity prices which are invariably linked to an improvement in demands from China (Figure 6). Once the stimulus package and monetary easing by the Chinese policymakers started to take hold, fixed asset investment in that country began to grow rapidly. The resurgence of investment there has in turn increased demand for raw materials, helping to boost trade balances of commodity-exporting countries like Indonesia and Australia. Whereas the current account's successive deficits in the second half of 2008 contributed to a depletion of Bank Indonesia's foreign exchange reserves and helped to foster perceptions of increasing country risks, its decisive swing into positive territory (and remained there) has done the exact opposite and stokes the current of optimism about Indonesia's prospects.

Domestically, the rounds of elections this year culminated in the re-election of market-friendly President Susilo Bambang Yudhoyono with an overwhelming direct mandate, as well as a strong showing for his Democrat Party in the earlier parliamentary elections. This has lent hope to the notion that the election results will enable his administration to have a stronger platform to undertake tough reforms that are essential for the country's economy. Globally, the major central banks managed to resuscitate the financial markets through a combination of rapid interest rate cuts as well as less-conventional quantitative easing measures.

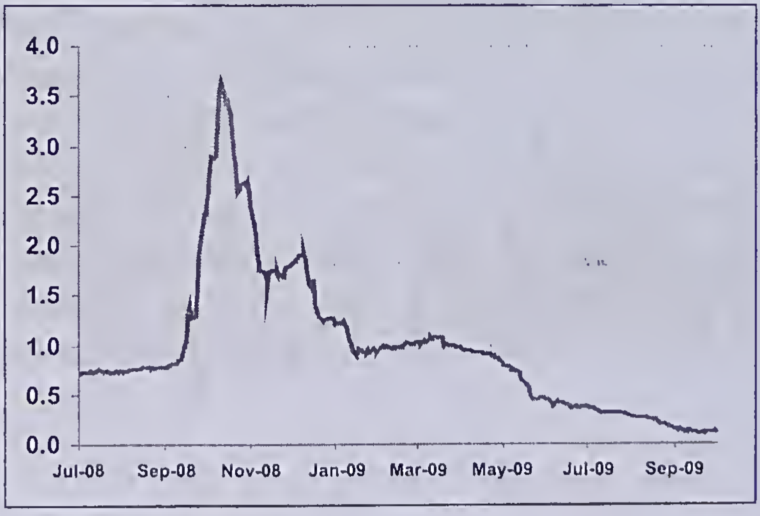
Figure 6: Export Drivers



Source: CEIC Asia Database

Banks started to lend to one another again, as they overcome the initial deep distrust of the creditworthiness of their counter-parties. The keenly watched Libor-OIS spread, which at one point shot up to as high as 3.64% in mid-October last year, began to make its gradual decline. By late August this year, the measure has dipped below 0.25% which according to Alan Greenspan, indicated that the willingness of banks to lend to one another has reached a 'normal' zone (Figure 7) (Fitzgerald 2009).

Figure 7: Libor-OIS Spread



Source: Bloomberg.

The return to a greater degree of normality in the global financial markets during the second half of 2009 has had a direct implication on the Indonesian economy. As markets switched from thinking about "returns *of* capital" back to the more normal assessment of "returns *on* capital", money began to search for yields and started to return to Emerging Markets, including Indonesia. The country has gained additional visibility in this environment due in part to its status as being one of the few major Asian economies to have maintained positive growth throughout the post-Lehman global turmoil. This has invariably led to optimistic portrayal of the country's prospects going forward, so much so that Moody's decided to upgrade Indonesia's ratings to Ba2 from Ba3 in September. By October, Standard & Poor's, while keeping its BB- rating for the country, upgraded its outlook from "Stable" to "Positive" in what is widely viewed as a precursor to a ratings upgrade.

Such optimism had played an important role in the dramatic shift in the country's capital accounts balance, particularly on the portfolio investment front. Portfolio flows have swung from the USD4.4 billion outflows during the global panic of the fourth quarter of 2008 into a decisive surplus of USD1.9 billion by the first quarter of 2009. The inflows have continued to strengthen since, registering net surplus of USD3.4 billion in third quarter of 2009. The scale of capital inflows has invariably contributed to a rally in the Indonesian stock market of late, enabling the index to be one of the best performing ones among Emerging Markets this year.

Foreign direct investment (FDI) inflows, however, have not been as ecstatic as portfolio investment. After the relative resilience throughout the tumultuous global events last year, FDI inflows began to taper off this year, with a mere USD0.4 billion received in the third quarter of 2009. One likely explanation is that potential investors are adopting a wait-and-see attitude towards the new cabinet team and its general policy directions. However, as will be explored later, we believe that there is a number of nagging structural impediments, such as inadequate infrastructure, that has inhibited Indonesia from attracting substantial FDI inflows.

NAVIGATING DOMESTIC MONETARY AND FISCAL POLICIES IN THE MIDST OF GLOBAL FINANCIAL CRISIS

It has now been well documented that the present global financial turmoil presents emerging market economies with two shocks, namely a sudden stop of capital inflows resulting from the global deleveraging process, and a collapse in export demand associated with the global recession (Ghosh, *et.al.* 2009). To mitigate the impacts of the two externally originated shocks, the country's management of macroeconomic policy responses, particularly those of monetary and fiscal measures, is crucial and has often been underlined as a detrimental factor in explaining the overall strength of the economy. This section would review key macroeconomic policy responses in Indonesia and generate lessons from them, in particular on the overall limitations of the macroeconomic policies during a global financial crisis.

Monetary Policy Side

As in advanced economies, the basic thrust of the monetary policy in Indonesia is to ease the impacts of the deleveraging process in the global economy on the domestic liquidity. Like many central banks around the world, Bank Indonesia (BI) had embarked on massive expansionary monetary policy measures. Its key policy rates declined from 9.5% in December 2008 to 6.5% in August 2009, and the rate is expected to be kept for the rest of 2009. BI also took measures to ease pressure on the bank liquidity by cutting the reserve requirement for bank's reserve at 5% from 9%. To help instil confidence in the domestic banking sector, the monetary authority raised the deposit guarantee limit from IDR100 million to IDR2 billion.

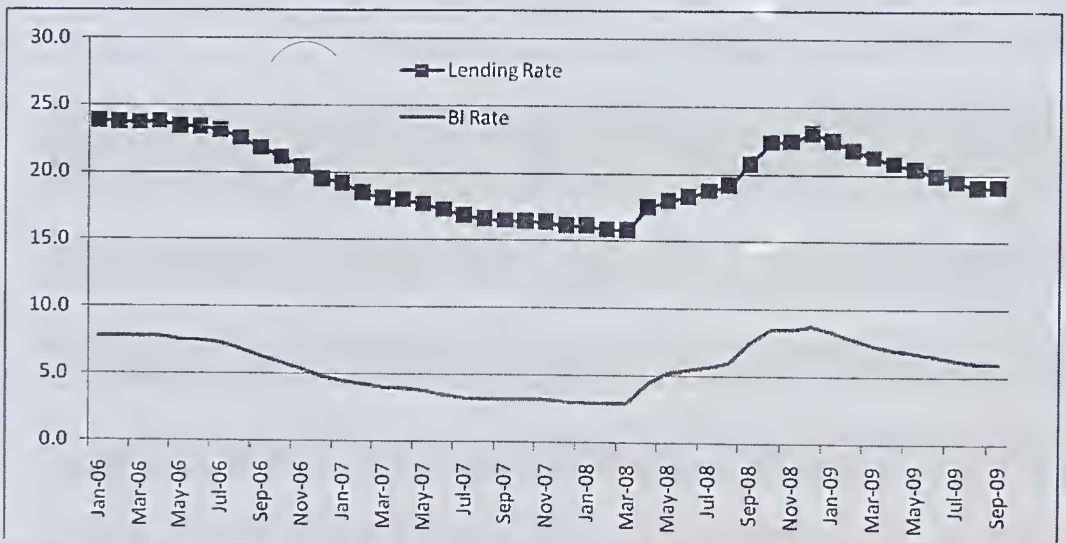
Yet, despite the expansionary efforts, lending rate declined only moderately, especially compared to that of deposit rate. At the end of July 2009, the interbank rate in Indonesia stood at around 7%, among the highest in the region. It is worth noting that the rise in the gaps between the policy rate and key market rates has been a common feature of financial crisis.[2] The policy rate, also known as the BI rate, was hovering around 8.5% in October 2008 and the spread rate between BI rate

[2] Similar episodes have also been reported in Indonesia during the 1997 financial crisis (Siregar 2005).

and the lending rate of the commercial banks was reported at around 5.4% during the same period (Figure 8). In September 2009, Bank Indonesia had reduced its policy rate to around 6% to help stimulate the economy, yet the spread rate had actually inched up to over 7%.

Market risk has often played a key role in explaining the widening gap between policy and market interest rates during the past financial crises (Taylor 2009). Reviewing the spread between the emerging market bond index (EMBI), capturing the expected cost of capital above the t-bill rate that a country must incur, Indonesia has indeed faced the most severe rise in the cost of borrowing at the global market. The country's EMBI rose above 800 point at fourth quarter of 2008, among the highest in the South-East Asian region (Table 2). The period of high EMBI also coincided with the sharp weakening of the local currency against the US dollar (Figure 1). Yet, despite the return of market confidence and positive outlooks in the domestic economy, the EMBI at the third quarter of 2009 still doubled the index at Q-2 of 2007.[3]

Figure 8: BI Rate and Lending Rate



Source: CEIC Asia Database

The widening of the interest spreads between the policy rate and the key market rates could adversely affect 'the optimal response of

[3] In September 2009, the Moody rating agency has upgraded Indonesia's foreign and local-currency sovereign debt ratings to Ba2 from Ba3.

the policy rate' to inflation, output gap and exchange rate volatilities. As market rates become less sensitive to changes in the policy rate, we would be in a situation where it would take much steeper adjustments in interest rate to have any meaningful impacts in the market (Siregar and Goo 2009). If the problem persists, the situation worsens and/or no more room to adjust the policy rate (hitting the 'zero' floor of nominal rate), monetary policy may end up to be completely futile.[4]

One key indicator, frequently found at the centre of the debate on the effectiveness of monetary policy in Indonesia, has been the growth of credits extended by the banking system in Indonesia. Despite the expansionary monetary policy position, the lending growth declined significantly from the peak of close to 40% per annum recorded in October 2008 to less than 10% by September 2009. Looking at the lending activities by the different groups of banks, only the state bank has been found to continuously sustain a high growth rate of credit at around 18% year on year at the end of September 2009. In contrast, the private commercial banks and the foreign banks recorded a dismal performance of around 4.5% and -5.4% in September 2009, respectively.

Table 2: Emerging Market Bond Index (EMBI)

	Indonesia	Malaysia	Philippines	Vietnam	China
Q1-2007	186	72	180	122	53
Q2-2007	144	71	138	101	52
Q3-2007	234	109	204	178	87
Q4-2007	271	120	208	203	121
Q1-2008	321	143	272	278	152
Q2-2008	338	141	244	366	132
Q3-2008	398	172	293	389	174
Q4-2008	837	396	566	797	230
Q1-2009	788	350	452	657	178
Q2-2009	419	179	301	353	87
Q3-2009	309	178	271	330	98

Source: CEIC Asia-Database

[4] The ineffectiveness of the monetary policy during the recent crisis, as captured by the widening of the interest rate gaps, is also evident on the experiences of developed economies. Martin and Milas (2008) demonstrate the case of United Kingdom.

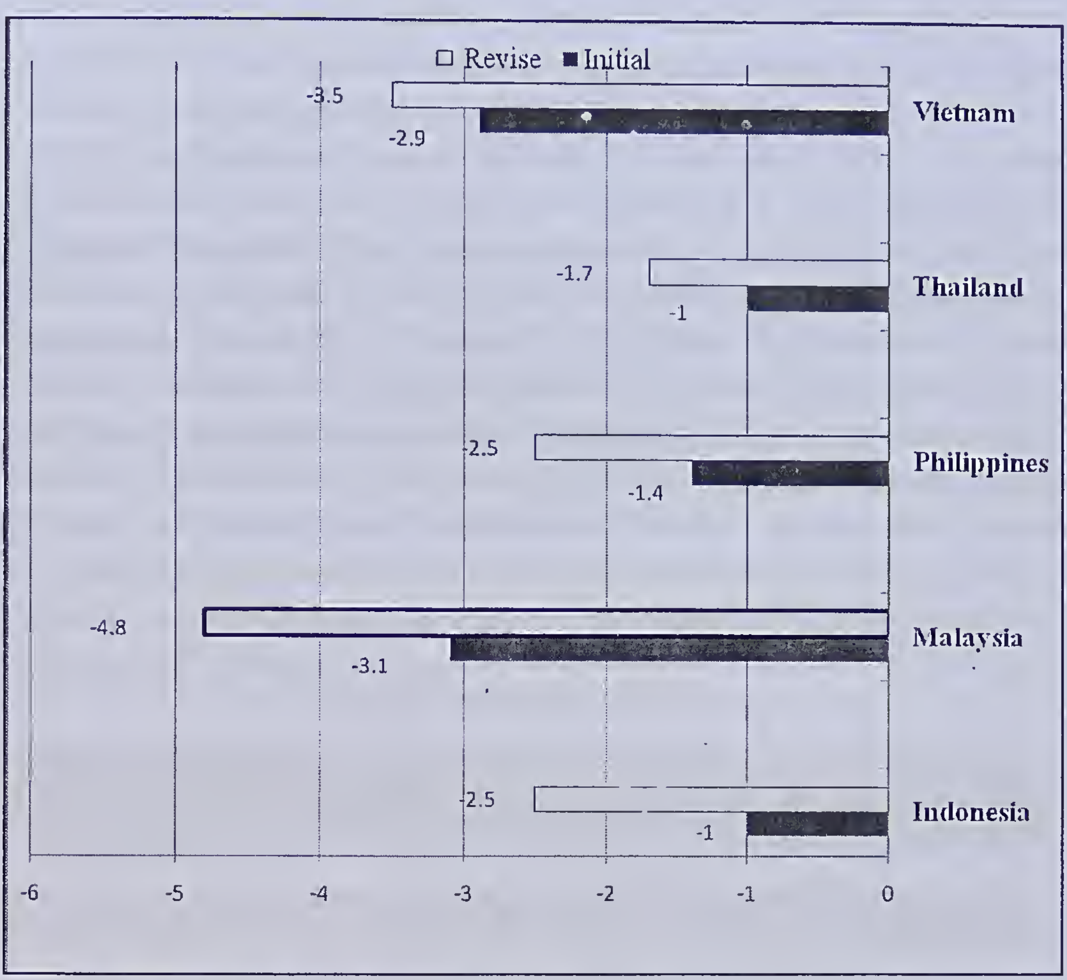
Counter-Cyclical Fiscal Stimulus

The past episodes of sudden stops have demonstrated that countries with tighter fiscal policy experienced sharper contractions than those with a looser stance (Ortiz, *et.al.* 2009)). Particularly, given the limitation of the monetary policy discussed earlier, the role of fiscal stimulus is critical, not only in terms of minimizing the impacts of the crisis, but more importantly in stimulating economic recovery. Facing drastic changes in the amounts allocated for energy subsidies, a rise in the fund needed to cushion the impact of global financial crisis, and a potentially much slower economic growth, the government of Indonesia has resorted to Article 23 of Law 41/ 2008 to facilitate access to the parliamentary hearing on the 2009 budget in mid-January 2009. Article 23 of Law 41/2008 stipulates that the government can return to the parliament and proposes for budget revisions under three circumstances. First, economic growth is expected to fall more than below 1% of the assumed growth, and other key macroeconomic indicators deviate more than 10% from initially projected. Second, there is a sharp decline on the third-party liabilities of the banking system. Third, there is a drastic rise in the yields of the government bonds.

The Minister of Finance unveiled a stimulus package for 2009, worth around IDR73.3 trillion (or around USD6.4 billion), to boost the economy amid the threat of economic downturn. The package is broken down into three major categories, namely income tax cuts, waives of tax and import duties, and subsidies and government expenditure. Aiming to stimulus more spending by the household and corporate, around 60% of the Indonesian fiscal stimulus has been allocated to cover cuts in income taxes. To minimize the effects of the global financial crisis, the government cuts individual income tax from 35% to 30% as well as corporate income tax from 30% to 28%. Recognizing the high dependency of the local industries (both on tradable and non-tradable sectors) on imports, as discussed earlier, around IDR2.5 trillion would finance waives of import duties for raw materials and capital goods. This is part of over IDR13 trillion package on tax and duties, about 18% of the total stimulus package, to predominantly support businesses. To help reduce the operation cost of businesses, the stimulus package also covers diesel and electricity subsidy. Last but not least, close to

IDR12.2 trillion will be allocated to support infrastructure and rural sector development.

Figure 9: Budget Deficit (in % of GDP) for 2009



Source: Bloomberg, CEIC Asia Database

In view of the measures above, the government has committed to raise its fiscal deficit to 2.5% of GDP in 2009. The flexibility of the Ministry of Finance to revise and to more than double the initial committed expansion highlights the successful effort by the country to reduce public debt and thus create the necessary fiscal space (Figure 9). At the end of 2000, the public debt level was reported to be close to 90% of the GDP. By September 2009, the country has seen its public debt level to drop to 30% of the GDP. Furthermore, the country's revised target rate of budget deficit is well within the ranges of the expanded fiscal stimu-

lus carried out by neighbouring Southeast Asian economies (Figure 9). At the highest end, Malaysia has amended its stimulus package and aimed at around 4.8% budget deficit for 2009. As one of the worst-hit economies by the recent global slowdown, Vietnam projected a budget deficit of around 3.5% in 2009. Facing limited fiscal space, Thailand had committed the most modest budget deficit at around 1.7% of GDP.

However, critics have long been pointing out that the government of Indonesia has often underestimated tax revenue growth, while over-estimating its ability to targeted projects. The speed of government spending continued to be hampered by bureaucratic inefficiencies, and lack of institutional capacity, partly due to the devolution of power to provincial and district-level governments in recent years. At the end of 2008, the budget deficit was only of 0.1% of GDP, much lower than its 2.1% target. In November 2009 hearing before Commission XI of the Parliament, the Minister of Finance reported that only less than 45% of the total stimulus package has been fully disbursed in the economy. On the expenditure stimulus, initially targeted around IDR12.2 trillion, the estimates show that only around 36% of the total amount has been fully absorbed by the local economy. The shortcoming is found in almost every key ministries and government agencies. For instance, the Ministry of Public Works has been allocated a stimulus package of around IDR6 trillion, and yet only 44% has been implemented by end of third quarter of 2009. Similar trends are reported from the other key ministries, such as the ministry of energy and mining, the ministry of agriculture, and the ministry of trade. The most encouraging result was reported by the ministry of health, with over 75% of allocated package fully disbursed.

Similarly, by July and December 2008, the regional government of the capital city, Jakarta, for instance, had managed to disburse only 17% and 64% of its annual budget, respectively (Basri and Siregar 2009). Two factors were blamed for this: the late budget approval and fears of improper disbursement following the Supreme Audit Agency's discovery of irregularities in the 2007 budget. Despite some improvements in the submission of the approved local government budget for the last two years, we still see that quite a few local government budgets (APBDs) were not approved until later in the year. Until end of January 2009, only around two thirds of the total local governments,

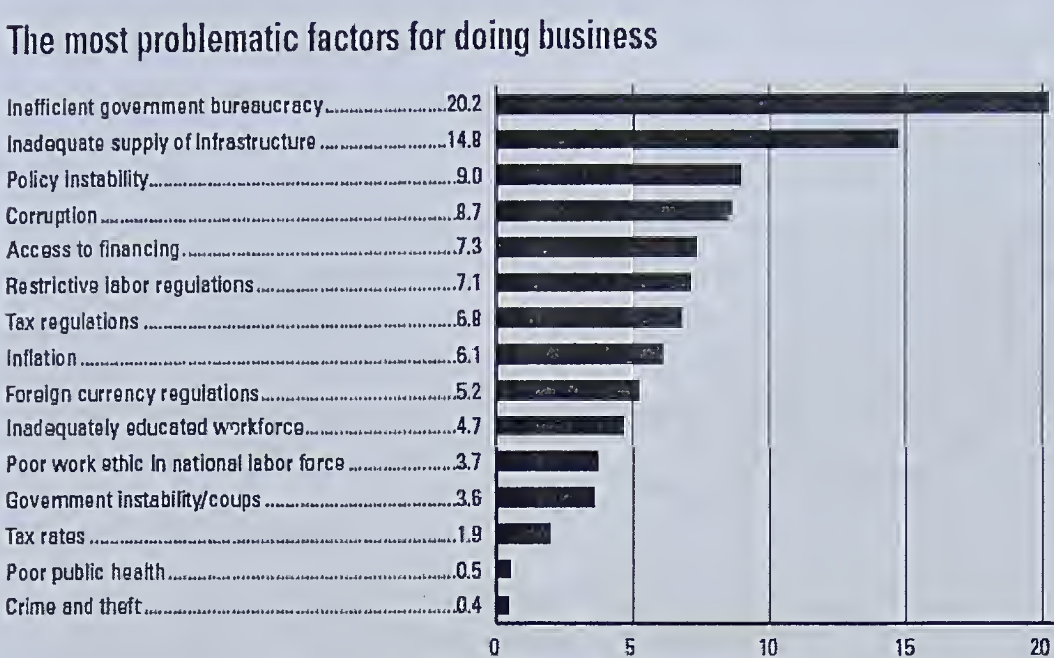
or 318 local governments, have reported the finalization of their 2009 budgets, and more than 192 local governments have not reported the finalization of their budgets to the central governments (Gunawan and Siregar 2009).

The fiscal effort has however been benefited from the two elections, the parliamentary and the presidential, taken place in 2009. In their recent study, Resosudarmo and Yusuf (2009) highlight the stimulus consequence of the election-related spending of the government. It is estimated the total election budget for both parliamentary and presidential elections was around IDR47.9 trillion, of which about IDR18.6 trillion was included in the 2008 budget and IDR29.3 trillion in the 2009 budget. It is estimated that the government spent about IDR50 trillion over a period of one year, compared to around IDR1000 trillion of total government expenditure in 2008. In other words, financing election expenditure should have boosted government spending by around 5%.

DISMAL STAGE OF INFRASTRUCTURE

Going forward, the dismal stage of infrastructure must be addressed for the country to have any chance in achieving its potential economic growth. The latest Global Competitiveness Report (the World Economic Forum (2009)) listed the country's inadequate supply of infrastructure as one of the investors' top-most concerns on the prospects of doing business in Indonesia (Figure 10). The problem of deficiency in infrastructure is worsened by the fact that it is wide-ranging, encompassing different aspects of infrastructure provisions. From roads to ports to electricity supply, investors surveyed by the World Economic Forum in its latest Global Competitiveness Report ranks Indonesia's infrastructure quality at 96th out of the 133 countries.

Figure10: Investors' Concerns about Doing Business in Indonesia



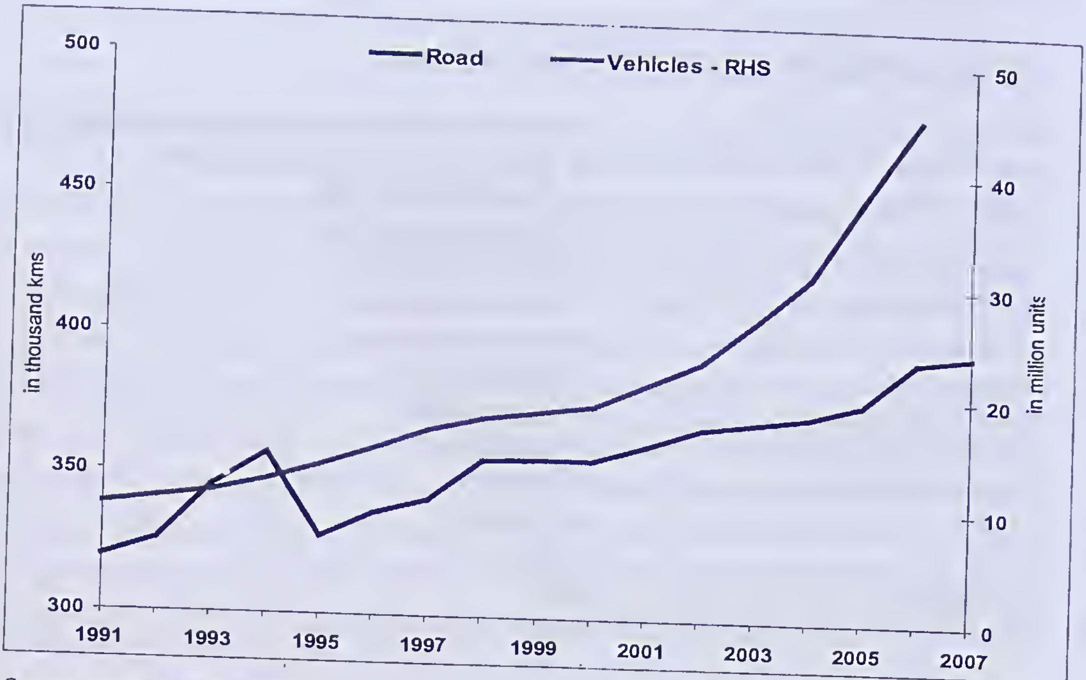
Source: Global Competitiveness Report 2009, World Economic Forum.

These findings demonstrate the dire state of the country's infrastructure. In many ways, the current inadequacy of infrastructure facilities in the country stem from the long period of under-investment by the government in the decade or so after the 1998 Asian Financial Crisis. According to a World Bank study[5], public infrastructure investment before the crisis stood at 5-6% of GDP. In the years after the crisis, this figure fell dramatically to about 1% of GDP in 2000. Although infrastructure investment has picked up since then, to about 3.4% of GDP by 2007, the amount of government spending on infrastructure is still significantly below the pre-crisis levels.

The minimal investment into road building, for instance, is unfortunately more of a norm than an exception. Between 1997 and 2006, the length of roads nationwide increased by a meagre 15%, with 52,000 kilometres or so being added. In comparison, the number of vehicles nearly tripled over the same period, increasing by as much as 28.5 million vehicles. The pace of increase in the provision of road facilities simply could not match the needs of the economy at all (Figure 11)

[5] World Bank (2007).

Figure 11: Road Transport Infrastructure



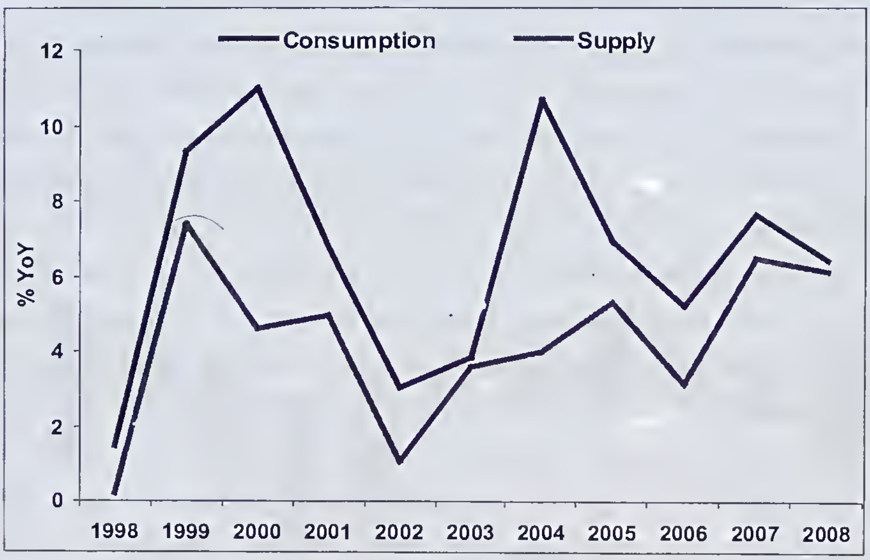
Source: CEIC Asia Database.

A similarly bleak picture can be witnessed in the electricity market. Between 2004 and 2007, electricity supply increased by an average of 3.4% per annum. Over the same period, however, demand for electricity accelerated at double the pace of supply, increasing by 7.6% per annum on average (Figure 12). There is little wonder then that latent blackouts plague many parts of the country, and have even started to occur on Java Island, which has traditionally been better off in terms of infrastructure provisions. Even the capital city of Jakarta, the nation's economic and political centre, has to suffer rolling blackout during the second half of 2009, much to the disappointment of foreign factory owners who have to contend with production disruptions.

All these deficiencies will make it that much harder for the country to attract and convince foreign investors to set up their factories and businesses. In an era where neighbouring countries are gearing up their efforts to capture the limited pool of foreign investments by offering a sophisticated set of incentive measures such as coordinated tax breaks and high-level infrastructure such as broadband connectivity, it is extremely unfortunate that Indonesia is struggling to even provide the very basic electricity and transportation needs.

To be fair, the government has been active in at least initiating a number of programs in their attempt to alleviate the infrastructure problems. During his first term in office from 2004-2009, President Susilo Bambang Yudhoyono's government had embarked on several initiatives to kick-start infrastructure development. In 2005, for example, the government announced plans to construct 1,000 kilometers of toll roads across the archipelago. A year later in 2006, the 10,000 megawatt power crash program was launched to meet the fast-growing demand for electricity. Some other key infrastructure projects that were initiated during this period include areas of public housing, water supply, and a particularly ambitious plan to install fiber-optic networks in all of the country's 33 provinces. [6]

Figure 12: Electricity



Source: CEIC Asia Database.

Progress has been painfully slow, however. Only 10% of the 1,000-km toll road project has been completed to date. The 10,000-MW Power Crash program looks to fare slightly better by comparison. Even then, only a quarter of the targeted capacity has been completed thus far. The major stumbling blocks affecting the progress of such infrastructure projects remain land acquisition and cost recovery uncertainties.

6 http://www.forbes.com/feeds/afx/2009/10/27/afx7046555.html

Land acquisition remains a major hurdle in road construction projects, particularly in the more densely populated Java Island. Acquisition of suitable land sites for projects are regularly hit with lengthy negotiations with residents, in part due to legal uncertainties on ownership of land.

Another major factor which has deterred would-be investors in infrastructure projects has been the lack of clarity on cost recovery after the projects are completed. Infrastructure projects require hefty initial investments that can only pay off in increments over extended periods of time after the completion of the projects. The pay-off for the investors comes in the form of electricity tariffs (in the case of power plant project) or tolls (in the case of toll road construction). These tend to be highly regulated by the government and are often subjected to politically-driven changes. As a whole, the situation adds to the degree of uncertainty and constitutes a deterrence factor for any potential investors.

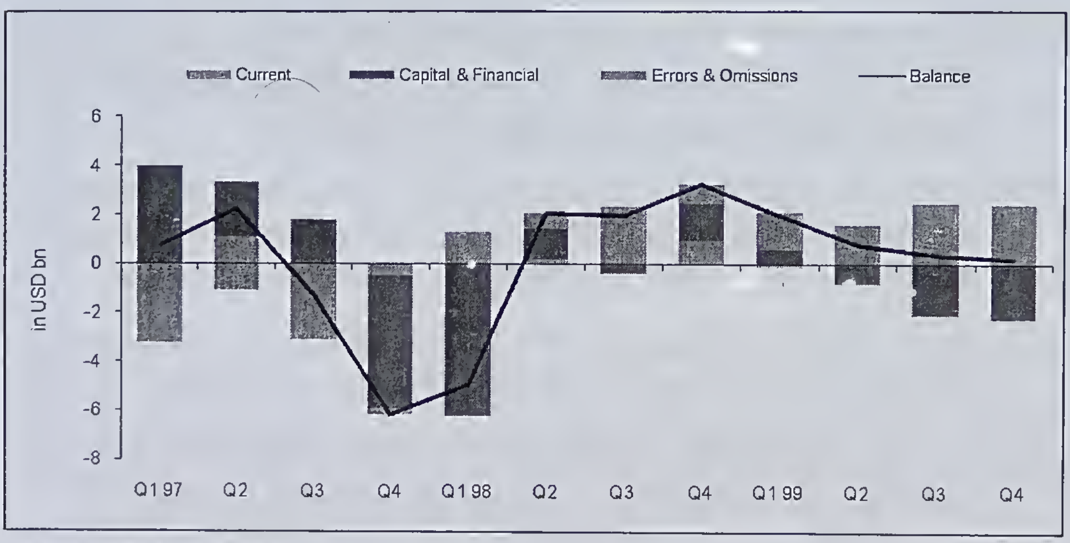
The president appears to understand such constraints well. Soon after assuming his second term in office, the buzzword for the new cabinet has been "de-bottlenecking". The government, rightly, sees the need to remove a number of constraints that have prevented the economy from enjoying a more rapid growth. As a reflection of the priorities they give to these issues, the president has even set up a new office called the Presidential Delivery Unit that is headed by a well-respected technocrat, Kuntoro Mangkusubroto. This office is singularly tasked with the removal of structural economic growth constraints, such as land acquisition mentioned earlier.

At the end of the day, implementation remains the key. Fruitful results cannot be accomplished by plans alone. The early signs may be promising. On the issue of land acquisition, for instance, the government is adding a new provision which would involve setting up a revolving fund to purchase land from the original owners, aiming to reduce risks for the investors. Foreign investors are watching the latest spurt of measures by the government closely, to see if the momentum of positive reforms can be sustained, and if the bottleneck of infrastructure inadequacy can indeed be removed. All eyes are on whether the president's second-term in office will yield more than the first one, in terms of improving the country's overall investment climate and attracting more direct investments.

CONCLUDING REMARKS

The Sub-prime financial crisis has abruptly and severely slowed the economic growth of many countries in the world, including the emerging markets in Asia (Table 1). It is therefore remarkable that the Indonesian economy has managed to continue to grow and avoid balance of payment crisis as in the 1997 East Asian crisis. The overall balance of payment of the country was in deficit only in the last quarter of 2008, driven predominantly by the sudden reversal of capital. In sharp contrast, the country had to endure persistently fragile balance of payment position for full two years after the initial outbreak of the previous East Asian financial crisis in the middle of 1997 (Figure 13). In addition, the country's relatively less reliance on trade and its diverse trading partners contributed to the strength of the country's current account balance.

Figure 13: Balance of Payment Position during the 1997 East Asian Crisis



Source: CEIC Asia database.

As found in other economies in different corners of the globe, the experience of Indonesia during the recent global financial meltdown has also accentuated the country's commitment to coordinated macroeconomic policies as a primary determinant of the robust economic growth. However our study has shown that the effectiveness of both monetary and fiscal policies has largely been hampered by a number of

limitations. Further studies, therefore, are warranted to examine how much the country's robust economic growth during the recent crisis has indeed been due to good policies.

Following the announcement of their election, President Susilo Bambang Yudhoyono (SBY) and his vice president, Boediono, promptly announced a set of socio-economic targets, including an annual growth rate of 7% by 2014 (the end of SBY's second term) and unemployment at around 5-6% (Resosudarmo and Yusuf 2009). It is clear however that the country must address its dire stage of infrastructure, if it were to have any real chance to achieve the set of targets outlined by the current government.

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THE SOCIO-ECONOMIC IMPACTS OF THE GLOBAL FINANCIAL CRISIS

Teguh Y Wicaksono and Raymond Atje

The global financial turbulence that originated in the United States has been translated into the decline of people's welfare. While in developed countries the financial crisis affects welfare through shrinking asset and jobs, in Indonesia the impact has been more limited. Indeed, when one makes a comparison between the current financial crisis and the 1997/1998 financial crisis, one could see some reasons to survive the impact of the crisis.

First, the current crisis began with a dramatic slump in asset values (e.g., mortgage crisis) in the US. In regard to this, Indonesia has successfully contained the current crisis as its banks and the financial institutions have no direct exposure to the US financial markets. This was completely different in the 1997/1998 crisis that created huge pressures on the exchange rate to depreciate significantly. Second, the lesson learned from the 1997/1998 Asia crisis has induced prudence into Indonesia's financial institutions. Third, policy makers drew from past experience about the need to maintain effective coordination among frontline ministers and Central Bank. These suggest that the government is better prepared to take the necessary policy responses.

However, the current crisis has greatly affected global economic growth, especially in Indonesia's major trading partners. This is how the crisis has affected the Indonesian economy, which in turn has its

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bearing on the country's poverty and unemployment landscape. To better understand the impact of the current financial crisis on poverty and unemployment, a review of the profile of Indonesia's poor is in order.

THE PROFILE OF INDONESIA'S POOR AND SOCIO-IMPACTS OF THE CURRENT CRISIS

The Profile of Indonesia's Poor

Poverty patterns after the 1997/98 crisis have not changed much[2]. Recent estimate suggests that the poverty rate in 2007 was 16.6%, already below that in 1996, which was around 17.5%.[3] In 2007 the level of absolute poverty, measured by the number of people living below PPP USD1 a day was 10.4%, or around 23.4 million. However, when measured by those living under USD2 a day, the number jumped significantly to 133.6 million or around 59.3% of the total population.

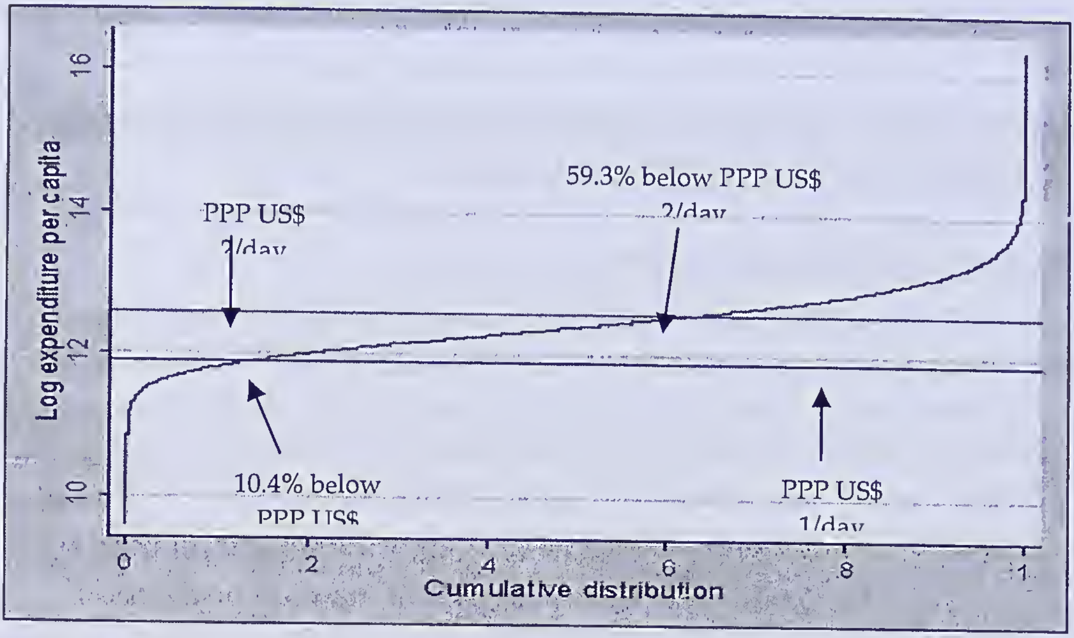
A doubling in the poverty line results in an almost five-time increase in the proportion of poor people. These figures suggest that a large number of Indonesians are living at near poor and are highly susceptible to adverse economic shocks. A negative shock, such as a large and sudden increase in the price of rice may send millions back into poverty. Such was the case when the poverty rate jumped from 16% in 2005 to 17.8% in 2006, resulting in an addition of more than 4 million poor people.[4]

[2] This section is largely derived from Atje, Soesastro and Wicaksono 2009

[3] Coordinating Ministry of Economic Affairs, "Evaluasi Ekonomi 2008 dan Prospek 2009", January 2009.

[4] Coordinating Ministry of Economic Affairs, "Evaluasi Ekonomi 2008 dan Prospek 2009," January 2009.

Figure 1. Cumulative Distribution of Expenditure per capita (Susenas 2007)



Source: Atje, Soesastro and Wicaksono 2009

The above shows that economic crisis may increase vulnerability of the people. However, it is also important to note that the major cause of economic crisis will determine the severity of crisis. Therefore, understanding the characteristics of poor people provides us with an insight on how such crisis affects welfare. As Indonesia is diverse in terms of the economic characteristics of the populace, an economic crisis could have different impacts on the people's income. For example, when exchange rate depreciates, people who earned their income from export-oriented commodities are relatively in better position than people working in industry that relies on imported raw materials. This diversity suggests the need for different approaches and policy measures in responding to an economic crisis.

Most of the poor in Indonesia live in the rural areas where one in every two households is poor. They are likely to be peasants, i.e., those who engage in low-paid agricultural sector jobs or small land holders. In addition, there are the urban poor whose number is smaller than the rural poor but, because of migration, is rapidly increasing. They are likely to be working in the informal sector or doing low-paid, me-

nial jobs in the formal sector. An adverse economic shock is likely to affect different economic sectors differently. The 1997/98 economic crisis, for example, had a greater adverse impact on the manufacturing, construction and financial sectors than on the agricultural sector. As a result, poverty incidence tended to increase more in the urban area than in the rural area. Nevertheless, the crisis might also have caused reverse migration from the urban area back to the rural area.

In terms of geographical distribution, poverty in Indonesia has a very strong geographical characteristic. Some of the remote regions, such as Papua, Maluku, East Nusa Tenggara, Gorontalo and Aceh, have higher poverty rates than the rest of the country. In these regions the poor households ranged between 20% and 41% of total households. The fact that these are remote regions suggests that their problem may be associated with the lack of access to market, resources, and various services.

Yet, the concentration of poor people in Java and Madura, where most of the Indonesians live, is much higher. The majority of poor people live in these two islands. A closer look at the concentration of poor people in Java and Madura shows that some of the districts in these two islands have average numbers of poor people similar to that of the remote areas mentioned above. It should be noted that the geographical characteristic of poverty in Indonesia has not changed significantly over the decades. That is, while the number of poor people has dropped significantly, their geographical dispersion remains the same.

As shown in Map 1, poverty rates are high in underdeveloped areas, (i.e., Eastern part of Indonesia and Aceh) which are sparsely populated, particularly in Papua. Meanwhile, as reflected in Map 2, the poor are mainly concentrated in Java and Madura—two islands with high population density. These geographical and demographic differences suggest that different poverty reduction strategies may be necessary to cope with the challenges.

In fact, this geographical distribution of poverty has been persistent for years and has not changed significantly. Economic shock may increase the number of poor people in some regions, but it rarely changes the whole picture of poverty in the country. A poverty map study undertaken by Smeru Research Institute in 2005 does not show

a much different picture from the current situation[5]. This finding supports the view that there are two necessary policies: (1) poverty reduction programmes addressing those who have been persistently in poverty; and, (2) social safety programmes intended for the "new poor" resulting from the economic shock. These two programmes have different characteristics and they work for particular regions with specific measures.

For example in the context of Eastern part of Indonesia, a specific policy for that region can be reached by universal poverty alleviation policy. Strengthening "common institutions" by providing universally basic services, namely healthcare and education in this region, would allow people to create new opportunities and, in turn, economic centers. Moreover, another challenge for the policy makers is to integrate the economies in the Eastern regions to nearby leading areas. Well-educated people always seek for better opportunities. Unless mobility factor (i.e., labour) happens at a reasonably low cost, the human capital investment would be wasteful. This implies that infrastructure to encourage people's mobility between the islands should be an integral part of promoting "common institutions." Yet, given the sparse population in Papua, infrastructure projects would hardly capture economies of scale, thus resulting in projects that are quite expensive and, perhaps, not feasible. Therefore, the challenge for policy makers is to find the sort of infrastructure projects that help integrate islands in this region.

On the areas with dense population, however, targeted policies become feasible and perhaps necessary. Java and Sumatera are regions with dense characteristic and have long been the pull-regions that attract people from all over the country.Likewise, Java has experienced large transformation from agriculture to manufacturing. Though large proportion of population still work in the agricultural sector in Java, cities with growing manufacturing sector have absorbed workers from the rural areas. They move from low-productivity agricultural sector to relatively high productivity manufacturing. Yet high level of migration

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[5] Asep Suryahadi, Wenefrida Widyanti, Rima Prama Artha, Daniel Perwira, Sudarno Sumarto, "Developing A Poverty Map for Indonesia: A Tool for Better Targeting in Poverty Reduction and Social Protection Program," A Smeru poverty map study. Current poverty map is based on a study by Raymond Atje, Hadi Soesastro and Teguh Y Wicaksono.

to cities that is accompanied by slow infrastructure adjustment has led to the creation of poverty pockets in urban areas. This creates challenges regarding inequality and has magnified the social-dimension issues. Sumatera, on the other hand, has transformed into a cash-crop production center, thanks to commodity booms. Some parts of Sumatra have also become manufacturing areas, for example Medan with its textile and garment industry. Cities in Sumatera are also growing and as Map 2 shows, they encounter the same poverty problem as in Java.

Map 1. High Poverty Rate in Eastern Part of Indonesia and Aceh

Map 2. High Concentration of the Poor in Java and Sumatera

Atje, Soesastro and Wicaksono 2009

The Socio-Impact of Current Crisis

How would the current economic crisis affect poverty and the employment level? The absence of high quality data to trace developments makes any shortcut assessment rather difficult. During the 1997/98 economic crisis, the government and aid institution undertook significant data collection to monitor the socio-economic impact of crisis. Several household surveys allowed us to figure out the progress of household income.

In spite of unavailable high quality data to assess the impact of current crisis, the cause and magnitude of the crisis could still enable us to make some prediction. First, the current financial turbulence might have a direct effect on the modern sector, such as financial institutions. Hence, , we might say that the impact of the crisis has only a marginal effect on the number of poor people as the poor people mostly accrue their income from agricultural or traditional sectors. Our experience in the 1997/1998 shows that the socio-economic impacts of the crisis on Indonesia's households were very heterogeneous. During 1997/98, incomes of some people working in industrial sector were pressured downwards by a dramatic depreciation in the exchange rate, which led companies to lay-off workers, whereas incomes of people working in cash-crop agricultural sector benefited from the depreciation.

The current financial crisis shows a similar pattern. Before the sub-prime mortgage market bust in the US, the world saw considerable increases in commodity prices. Households in some parts of Indonesia benefited from the increase. This has raised income of people who work in export-oriented commodities, particularly outside of Java Island. However, by the end of 2007 food prices increased significantly, which kept pressures on purchasing power. The most affected population from this shock is the poor living in Java, particularly those who work in food-crop production with low values. Based on this observation, it is rather clear that households in Java are affected most by the crisis.

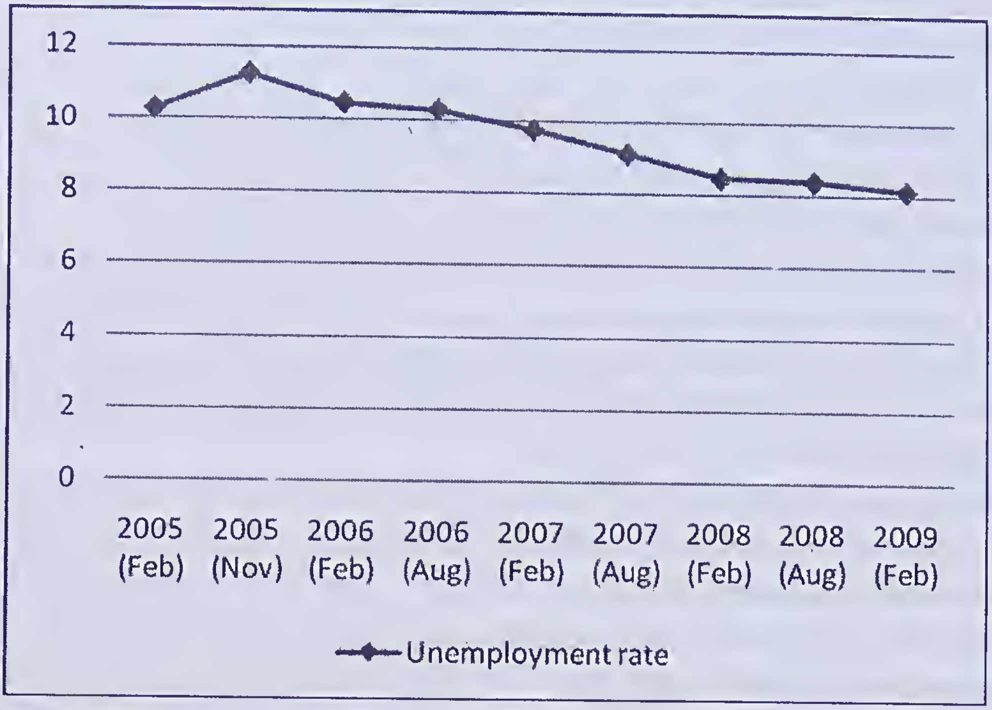
Second, as the current financial crisis affected Indonesia's major trading partners, the industrial sector, particularly export-oriented manufacturing, experienced a decline in external demand. This could have a direct impact of people working in the manufacturing sector.

However, strict labour regulations imposed since 2003 have led manufacturer to hoard its worker amid declining demand[6]. At the same time, the regulations already changed the way employers are hiring their workers. To get around the regulations, most employers prefer to offer contract job for 6-month rather than offering permanent job to a worker. They also prefer to outsource several production activities. This has led to more fluidity of job flow, and unfortunately this cannot be captured by the national data. As a result, we observe a relatively unchanged unemployment rate as the crisis begun. Yet, even if the crisis takes victims, it is very likely that people living on Java (particularly in urban area) and working in export-oriented manufacturing sector are the most affected by the crisis.

Figure 2 clearly shows that unemployment rate has declined significantly since November 2005. The continuous decline of unemployment rate consistently followed robust economic growth during the 2005-2009 period. Besides, a dramatic decrease in unemployment rate also took place in the same period in which economic growth recorded the highest rate since 2003. It suggests that the employment rate-growth elasticity is relatively high (i.e., economic growth is sensitive to boost employment rate).

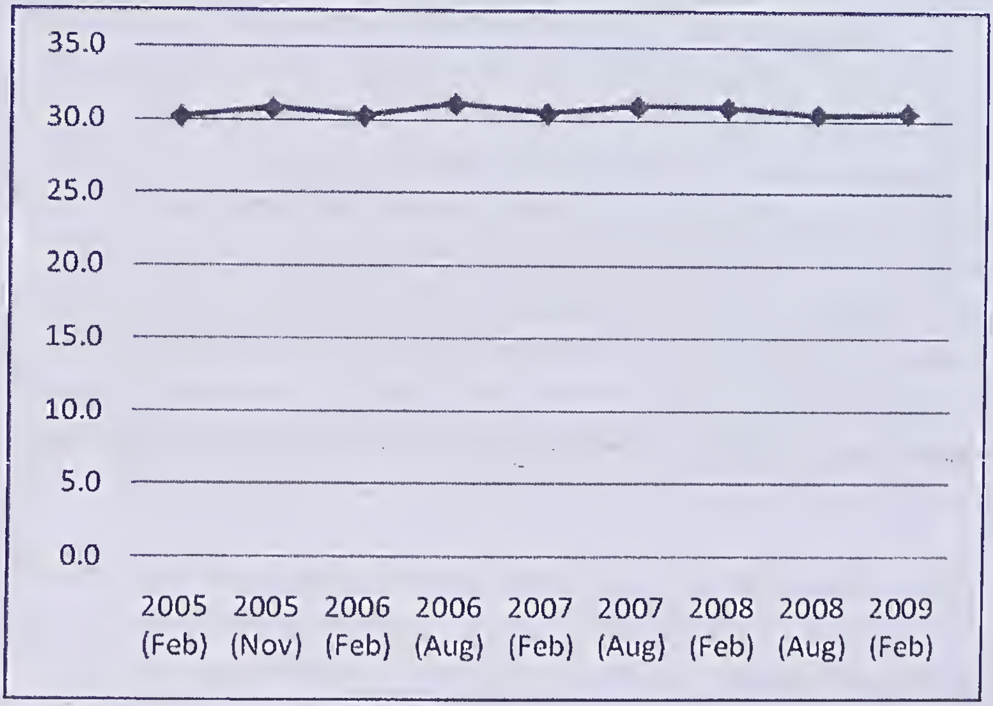
[6] The government introduced the Manpower Law No 13/2003 which is considered stricter than the previous one.

Figure 2. Unemployment Rate (%)



Source: BPS

Figure 3. The Percentage of Formal Sector

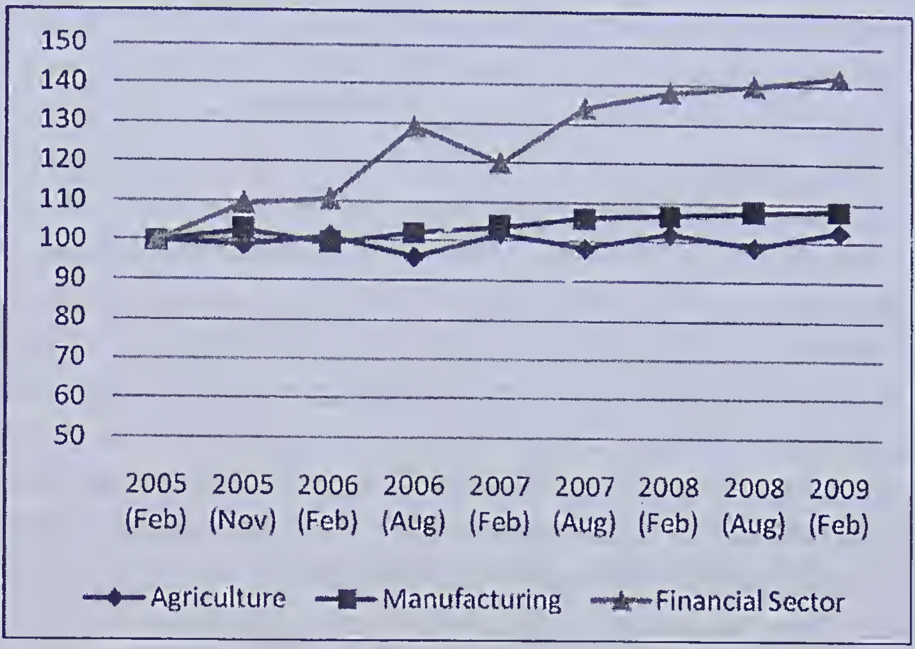


Source: BPS

Although unemployment rates have continuously declined, there has been no significant improvement in labour market performance. The proportion of workers in the formal sector is around 30% of the total worker (see Figure 3). However, the other side of the coin of these figures is that the economic crisis in 2008-2009 has a limited impact on the labour market. It is also important to note that employment data in February 2009 might not capture the impact of the crisis as yet. Figure 4 seems to question our presumption about the impact of the crisis on labour market performance[7]. While the crisis is predicted to keep workers in the financial and manufacturing sectors off work, data show us that the employment levels in these two sectors (financial and manufacturing) are likely to grow. Indeed, employment in the financial sector grew rapidly in the 2007-2008 period. Employment level in manufacturing sector also increased slightly in the same period, even though the manufacturing sector has been the hardest hit by the current crisis. The behaviour of firms hoarding employment explains why employment level slightly grew despite the decline in demands for manufacturing output.

[7] A current study by ILO Jakarta office reported that employment informal sector grew dramatically from 61.3 percent (February 2008) to 67.9% of total employment (February 2009)-or increasing by 6.6 percentage point). This finding is likely to conclude that the impacts of crisis have extended to labour market performance. However, our figure based on BPS data shows that informal sector by February 2009 was higher that ILO's figure (69.5%). This percentage was similar to the figure in February 2007—the period of solid economic growth. It is also worth noting that the sample size of labour force survey in February is smaller than that in September, suggesting the presence of a sampling size issue. In other words, a slight increase in informal sector employment could be attributed to sampling size issue instead of indicative measure of informal employment (A study by ILO is quoted from Antara News).

Figure 4. Index of Manufacturing Employment (2005-2009)



Source: BPS

Judging from Indonesia's macroeconomic condition in 2008, the current situation is far better than that in the 1997/98 financial crisis. The economy continued to grow although at a slower pace. A mild effect of the crisis on poverty is reflected by current data on poverty. By 2008, the poverty rate had continued to decline both in urban and rural areas. The continuing decline in urban poverty rate shows that the impact of the current crisis has been relatively more contained than many observers have thought.

Table 1. Number of Poor Population, 2006-2008

Year	Poverty Line (Rupiahs/capita/month)		Population below the poverty line million	
	Urban	Rural	Urban	Rural
2006	174,290	130,584	14.5	24.8
2007	187,942	146,837	13.6	23.6
2008	204,896	161,831	12.8	22.2

Source: BPS-Statistics, 2008

SPECIFIC IMPACTS OF THE CRISIS ON EDUCATION AND HEALTHCARE SECTORS

An economic crisis obviously affects the living standard of households. However, it also has intertemporal effects on current household consumption and in turn intergenerational consumption. For example, households which suffered a substantial decline in income tend to reduce spending on their children's education. Accordingly, this will affect children's potential income and consumption in the future. The magnitude of the 1997/98 economic crisis was devastating to Indonesia's macroeconomic situation. Unquestionably, the social impact of the crisis had triggered much controversy. Like what happened to poverty issues during the 1997/1998 crisis, alarming views on other social issues also entered the public debate. Politicians and media predicted about the possibility of losing a generation due to the economic crisis. Yet, this view was not supported by careful research and research findings, suggesting that households had been resilient during the crisis (Cameroon 2001).

Based on data from 100 village survey, Cameron found that the impact of the crisis on school attendance rates was mild. The attendance rate at primary level was not at the heart of the debate as Indonesia already achieved universal primary education. The downward trend of attendance rates was observed at secondary school level. By August 1998, the attendance rate for lower secondary was 65.2%, which was lower than the level of May 1997. However, by May 1999, the attendance rate rebound to the level of 69.7%. The same pattern occurred in upper-secondary level in which attendance rates dipped slightly and rose again by May 1999.

By region, rural areas experienced the larger decrease than did the urban areas at lower secondary level. Yet by May 1999, the attendance rate in rural areas rose to the level of May 1997. An upward trend in attendance rate also occurred in the upper-secondary level in the rural area. It is very interesting to note that urban areas experienced relatively a slight decrease in the attendance rates of secondary level as urban households were expected to suffer greater impact of the crisis. This may also be caused by their perception that priority of household spending must be set to education.. Households in both rural and urban areas also proved themselves to be tough in the face of hard economic condition.

In the context of gender, attendance rates of female in lower secondary level suffered the larger decrease than that of the male. Using large-scale data (National Socio-Economic Survey/*Survey Sosio-Ekonomi Nasional*/Susenas), Levine and Ames reported that girls were not far worse than boys during the crisis, since both were equally well protected (Levine and Ames 2003). Their finding supported the view that gender-discrimination is non-existent in Indonesian education (Oey-Gardiner 1991, Cameron 2001).

Table 2. School Attendance, 1997-1999

	May 1997	Aug 1998	Dec 1998	May 1999
Entire sample				
Primary (6–12 years)	80.4	87.4	86.4	81.8
Lower secondary (13–15 years)	69.0	65.2	66.7	69.7
Upper secondary (16–18 years)	33.1	31.5	32.2	34.3
Urban/rural attendance				
Primary				
Urban	84.8	90.4	88.7	84.4
Rural	79.4	86.7	85.8	81.1
Ratio	1.07	1.04	1.03	1.04
Lower secondary				
Urban	80.6	77.8	80.0	80.9
Rural	66.0	61.9	63.3	66.8
Ratio	1.22	1.26	1.26	1.21
Upper secondary				
Urban	47.6	50.7	49.4	53.4
Rural	28.6	25.8	26.8	28.5
Ratio	1.66	1.97	1.84	1.87
Male/female attendance				
Primary				
Male	79.1	86.5	85.5	81.1
Female	81.8	88.4	87.4	82.4
Ratio	0.97	0.98	0.98	0.98
Lower secondary				
Male	67.5	65.1	66.4	68.4
Female	70.6	65.2	67.1	71.1
Ratio	0.96	1.00	0.99	0.96
Upper secondary				
Male	34.7	32.5	33.1	34.4
Female	31.5	30.5	31.2	34.2
Ratio	1.10	1.07	1.06	1.01

Source: Cameron, 2001

While the impact of the 1997/98 crisis on education was not so severe, the health situation even showed a substantial deterioration. A report by Frankenberg *et.al* which employed Indonesian Family Life Survey (IFLS) data stated that the proportion of adults using public healthcare service declined from 7.4% in 1997 to 5.6% in 1998. They also found that users were likely to shift away from Community Healthcare Centre (*Puskesmas*) to traditional practitioners. This shows that limited resources became the main problem for the poorest households in accessing healthcare services during the crisis (Frankenber *et.al* 1999).

The use of healthcare services for children also declined substantially. The study found that children health visits to Health Post (*Posyandu*) dropped significantly from 46.7% in 1997 to 27.7% in 1998. The poorer and middle income households switched-off the use of public health facilities. While visits to Health Post declreased considerably, the proportion of toddlers receiving Vitamin A also fell. The situation was getting worse as the cost of using public and private healthcare services increased due to inflation. It was found out that the driving forces which caused a deterioration of the health situation during the 1997/1998 economic crisis were: (1) the declining resources allocated to public healthcare services and the incomes of household; and, (2) a significant increase in the inflation rate, which led to the increase in healthcare services.

It was argued that the current crisis has no significant impacts on enrollment rates[8]. Although there are no careful studies on this issue, the impact of the current crisis is considered to be less severe than that in 1997/98. This is partly attributed to the government's decision to increase the budgetary allocation to education to almost 20%.[9] Though the increase is not a response to the crisis, a considerable increase in the budget has worked as a safeguard to keep students at school under whatever economic condition. As the trend of the education budget continues and at the same time the number of school-age children

[8] Based on our interviews with donor staff (e.g., UNICEF, UNDP)

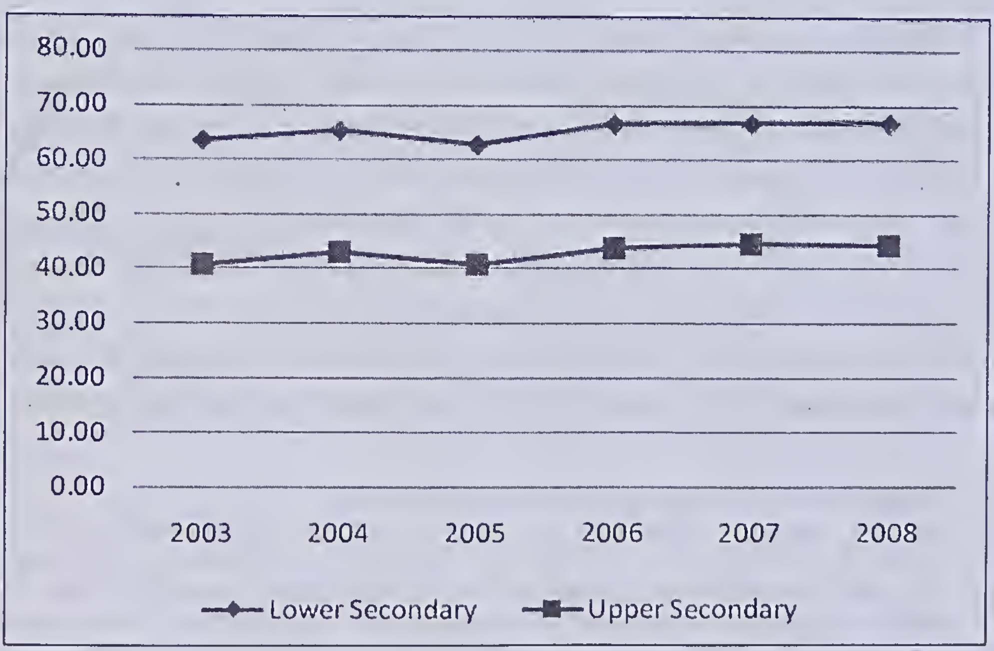
[9] Constitution stipulates that 20% of total government budget must be allocated to education sector. Though constitution mandates 20% of the total budget to be allocated to education, the government had argued that limited fiscal capacity does not allow the government to allocate the budget for education as mandated by constitution. By August 2009, the Constitutional Court stipulates that the government must allocate the budget for education according to constitution. The government then increased the budget allocated to education sector.

declined due to the successful family planning programme, the allocated education budget per child will also increase accordingly. This indicates that the government should design education policies aimed more at education quality improvement than at school infrastructure.

In addition, culture also contributes to parents' supportive attitude toward children education. Spending on education has been a high priority among Indonesia households. This attitude therefore becomes a significant factor that makes children remain at school in difficult times when the government faces limited resources. Participation among parents, community, and the government is required to maintain investment in human capital; and it is badly needed during the economic crisis. The current experience also shows that households have been resilient in facing difficult situations.

Figure 5 illustrates that net enrollment rates of secondary school have been stable between 2006 and 2008. It is worth noting that the 2008 data did not capture yet the impact of the crisis on enrollment rates. However, given the magnitude of the 2008 economic crisis, the impact on enrollment is more contained than it was in the 1997/1998 economic crisis.

Figure 5. Net Enrollment Rate of Lower and Upper Secondary Level (%)



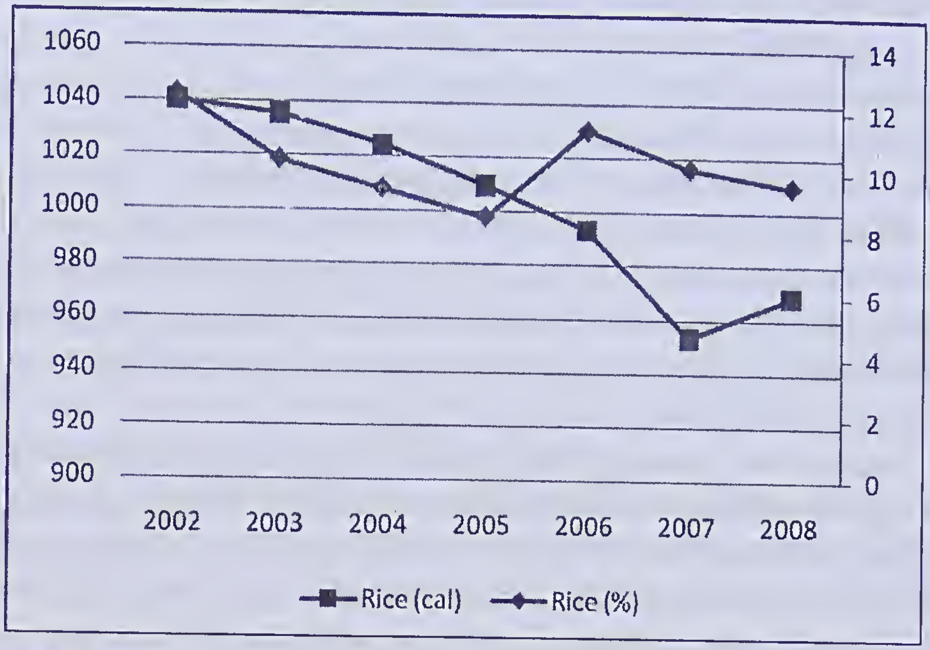
Source: BPS

Regarding the health sector, the impact of the crisis is less clear. Another possible cause to the deterioration in healthcare services could be increases in food prices preceding the crisis. Households have changed their behaviour in food purchasing from less-expensive but nutritious food (e.g. rich protein food like soy cake and eggs) to poor quality food.[10] This was also followed by a sharp decrease in the quantity of food purchased. Nevertheless, the impact of the reduced food intake on nutrition status is not well-documented due to the absence of the related data. Because of the prolonged malnutrition, the changing nutrition status of people, particularly children, could not be recorded. Surprisingly, families in vulnerable areas were found not in a catastrophic situation.

In spite of the increased food prices, the aggregate picture on food consumption exhibits that Indonesian households seem to consume more high nutrient food (see Figure 6 and Figure 7). While the proportion of per capita expenditure on rice declined in the 2002-2005 period, the calorie intake per capita on rice also decreased. At the same time, however, calorie intake per capita of other high nutrient foods (meat and fish) slightly increased. This illustrates that to some extent Indonesian households have changed their consumption pattern toward more nutritious foods. This trend became clear in the 2006-2008 period as households consumed more fish and meat. Price effect is one major reason for the change in the consumption pattern, as we witnessed that the percentage of per capita consumption on food of total expenditure tends to decline. In other words, a decrease in prices of food has increased purchasing power and led households to take more nutritious foods. This is reflected in Figure 8.

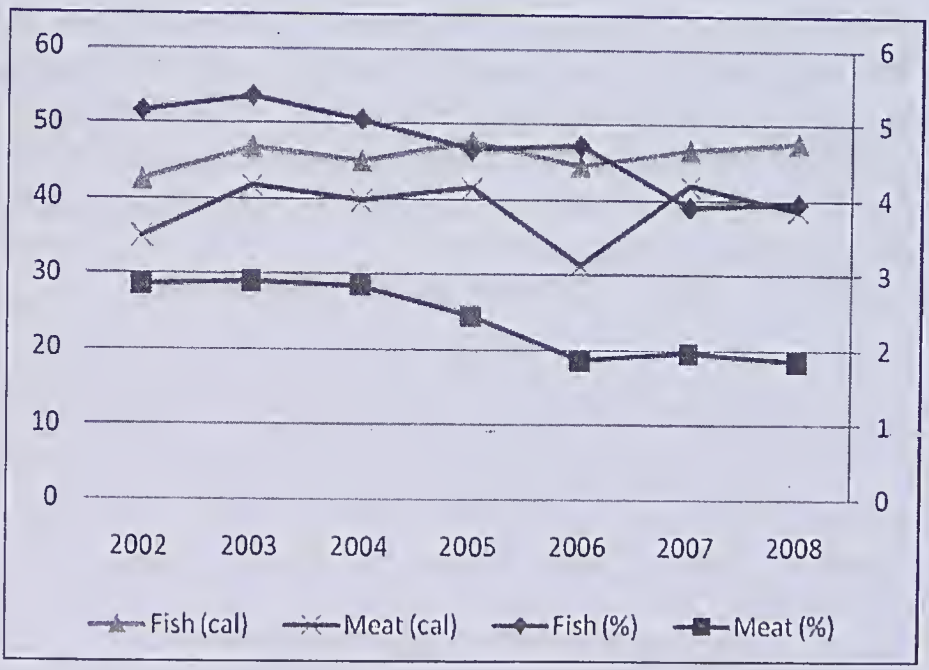
[10] Based on interviews with UNICEF staff.

Figure 6. Calorie Intake Per capita and the Percentage of Per capita Expenditure on Rice



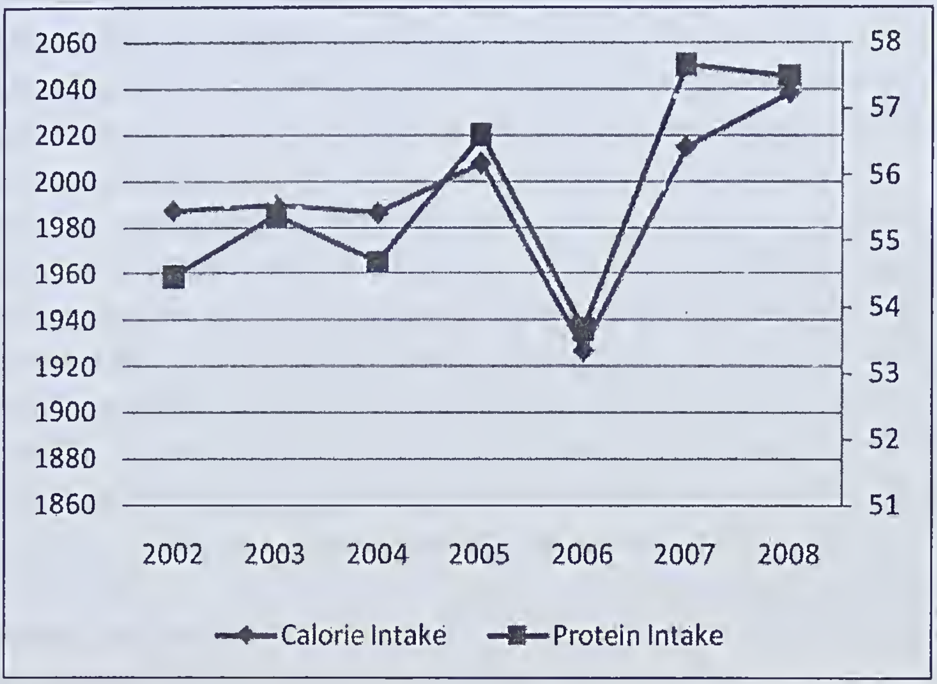
Source: BPS

Figure 7. Calorie Intake Per capita and the Percentage of Per capita Expenditure on Fish and Meat



Source: BPS

Figure 8. Calorie Intake Per capita and the Percentage of Per capita Expenditure on Fish and Meat



Source: BPS

In other words, the extent of the social impacts of the crisis has not been too bad thus far. Indeed, there is no decline in enrollment rates, suggesting that there are no major impacts of the crisis. Concerning the health sector, it is an increase in food prices rather than the current financial crisis that affects the health situation. Domestic food prices (particularly rice price) have been stable since 2008. That was indicated by the continuing downward trend of inflation from 2008 to 2009. As food prices have been maintained, subsequently constraint on households to purchase good quality food became lower.

RESPONSE TO THE CURRENT CRISIS: SOCIAL SPENDING

In the adjustment of the 2009 State Budget, the government has included social protection and poverty alleviation programmes. There are several social assistance programmes in Indonesia which could be categorized as social safety net and social rehabilitation programmes. Some of these programmes that were launched during the 1997/1998 crisis include: (1) subsidies; (2) social safety net programmes, such as

JPS-BK (healthcare), education assistance (BKM /*Bantuan Khusus Murid*/Students' Special Assistance) and BOS (*Bantuan Operasional Sekolah*/ School Operational Assistance, and food assistance (OPK/*Operasi Pasar Khusus*/Special Market Operation for Beras/Rice); and, (3) labour intensive projects, such as PNPM Mandiri/*Program Nasional Pemberdayaan Masyarakat Mandiri*/Independent People's Empowerment Programme.

Currently, some of these social safety net programmes are still carried out with few modifications in schemes and targeted recipients. Aptly named PKPS-BBM (*Program Kompensasi Pengurangan Subsidi Bahan Bakar Minyak*/Compensation Programmes in lieu of Reduced Fuel Subsidy), the scopes of programmes are similar: in healthcare (Askeskin), in education (BKM and BOS), food assistance (Raskin), and direct cash transfers (both conditional and unconditional). In addition, there are also social rehabilitation programmes targeted to natural disasters (earthquakes, floods, severe land slide) and other social problems, such as mass riots.

The 2009 Government Work Plan will be focused on Welfare Improvement and Poverty Reduction programmes. To carry out this work plan, the government has set up three development priorities: : (1) promoting basic public services and rural development; (2) encouraging inclusive growth; and, (3) improving anti corruption effort, bureaucratic reform and strengthening democratization.

In regard to promoting basic public services for the poor and rural development priorities, the activities cover: (1) developing and improving social protection system for the poor; (2) expanding community-based development program; and, (3) improving small-scale business development. Table 3 shows social protection programms that are partly aimed at developing and improving a social protection system for the poor. Additionally, there are four programmes taking the large share of social protection programmes, namely, community empowerment programmes (*Program Nasional Pemberdayaan Masyarakat*/ PNPM), subsidized rice for poor family, health and education programmes. It should be noted that the budget of some programmes—like education and health—is not only allocated under this sub-theme, but also in other sub-themes of the development programmes. The activities of this sub-theme are particularly intended to have direct impact on the poor.

On the education sector, all activities are in the form of scholarships worth IDR2.5 trillion (USD226.6 billion) in 2009. Free healthcare programme both in hospital and Community Healthcare Centre (Puskesmas) are activities of the health sector, worth IDR7.2 trillion (USD653.1 billion). The subsidized rice for poor family program is the largest among social protection programmes (IDR10.7 trillion or accounted for one third of total social protection programme).

Furthermore, between 2007 and 2009 there is an increasing trend in several social protection programmes mainly due to an increase in the number of beneficiaries. However, the striking change is in the health sector in which free healthcare facility in Puskesmas increased by 203% and the programme is expanded and not limited only to poor families.

Amid the slowing down of the economy, fiscal policy is expected to take a large role, suggesting the urgency of counter-cyclical policy. Yet, the current 2009 revised budget shows that fiscal expansion is limited. In terms of percentage to gross domestic product (GDP), the 2009 revised state expenditure is lower than the 2008 budget. Central government expenditure accounted for 15.5% of GDP, which is lower than that in the 2008 budget. The same situation is in the transfer of resources to regions. The lower ratio results in rather mixed expectation upon the objectives of the 2009 state budget, despite the recent fiscal stimulus package.

Two explanations can be offered here in regard to fiscal restraint. First, for the last five years, the ratio of non-discretionary expenditures to total expenditure has been increasing; mainly due to external changes (oil price and exchange rate). Rising non-discretionary expenditure portion can be partly attributed to subsidizing rich population at the expense of poor population (the case of gasoline subsidy). As of now, the largest spending item in the State Budget is education spending (as required by the Constitution, currently at approximately 17.2%). The next largest items were subsidies (15%) and government administration (15%). It is not surprising that fiscal expansion, if any, in the economy is very limited. To address this constraint, since 2007 the government has reallocated expenditure items from material expenditures (*belanja barang*) to capital expenditures (*belanja modal*) and social supports. It is expected that this reallocation would optimize expendi-

Table 3: The Expenditure of Social Protection and Direct Intervention Programme (IDR billion)

Programme	2007	2008		2009*	
	Budget	Beneficiary	Budget	Beneficiary	Budget
Community Empowerment Programme (PNPM)	3,500.2		6,114.3		9,410
Urban Poverty Reduction Programme	1,161.5	Direct support and technical assistance to poor community in 3,581 villages (keluharan)	1,414.7	1,072 sub-districts	1,737
Socio-Economic Infrastructure Development program	0.0	Technical assistance in 237 sub-districts	52.5	Technical assistance in 1,817 villages of 237 sub-districts	485.3
Lagged Area Development Programme	344.7	Direct support and technical assistance to poor community in 186 sub-districts in 32 district of 8 Province	363.0	51 districts, social support to 1,044 villages	195.9
Kecamatan Development Programme (Rural Development Programme)	1,994.1	Support to community in 2.389 sub-districts'	4,284.1	Support to community in 4,662 sub-districts	6,992
Subsidized rice for poor family	6,584.3	19,1 million families for 10 Kg rice	8,589.4	19,1 million families with20 Kg rice	12,909
Education	766.8		2,268.8		3,617.3
Scholarship for Primary School	0.0	1.258 million poor students	455.9	2.44 million poor students	877.2
Scholarship for Junior Secondary school	0.0	779.1 thousand poor students	556.7	1.54 million poor students	1,107.5
Scholarship for Senior Secondary School	680.0	930.8 thousand poor students	731.3	1.22 million poor students	956.9
Scholarship for Tertiary Education	86.8	214.0 thousand poor students	524.9	314.2 thousand poor students	675.7
Health	4,566.2		4,566.2		7,224
Free healthcare facility in hospital grade III for poor family	3,708.0	76,8 million poor families	3,708.0	76,4 million poor families	4,584.0
Free healthcare facility in Community Healthcare Centre (Puskesmas) for poor family	858.2	76,8 million poor families	858.2	All families deserved to basic healthcare facility in Puskesmas	2,640.0
Other Social Protection Programme	2,453.6		3,823.8		4,375.6
Total Social Protection Programme	17,871.2		25,362.6		37,535.9

*Indicative
Source: Bappenas 2009

tures, particularly at ministerial level, and is intended to have a greater direct impact on the public.

Second, the government seemed to lack the capability in spending resources, both at the central[11] and local level. Based on data from the Ministry of Finance, almost 30% of total government spending in 2009 (part of the stimulus package) would be transferred to local governments. By January 2009, only 57% of regions in Indonesia have submitted their budgets. Indeed, the delay of these budget submissions had posed serious problems. Fortunately, political campaigns for legislative and presidential election took place in the first half of 2009 and seemed to have compensated for the lack of government stimulus in cushioning the worst impact of current global crisis.

A striking feature of the 2009 revised budget is the dramatic increase in the budgetary allocation to education sector. In the proposed budget, the government allocated IDR69.0 trillion (USD6.3 billion) to education sector. In accordance with the Constitutional Court's decision, the government had to allocate additional budget to education sector by IDR46.2 trillion (USD4.2 billion) or an increase by 66.9%. Despite the Court's decision, the allocated budget to education sector is still lower than the mandated allocation. It accounts for 10.3% of total government expenditure or 14.1% of central government expenditure[12]. The central government argued that although the allocated budget to education sector in the 2009 government budget is still less than 20%, the sums of the budget at the central and local government combined are expected to reach 20% of total government budget. However, the evidence is unclear as the recapitulation of government expenditures at the central and local level is not made publicly available. Furthermore, the resources allocated to health and social protection increased slightly to IDR17.5 trillion (USD1.6 billion) and IDR3.4 trillion (USD0.3 billion), respectively.

[11] At one point of time (August 2008), central government account in Bank Indonesia (the Central Bank) accumulated IDR200 trillion of unused budget.

[12] The figures do not include the local government expenditures.

Table 4 The Central Government Expenditure by Function (IDR trillion)[13]

Sector	2005	2006	2007	2008 Proposed Budget	2009 Proposed Budget I	2009 Proposed Budget II
Public Services	255.6	283.3	316.1	518.2	660.1	565.0
Defence	21.6	24.4	30.7	10.5	13.8	13.8
Home Security	15.6	23.7	28.3	12.3	15.7	15.7
Economy	23.5	38.3	42.2	57.2	58.9	58.9
Environment	1.3	2.7	5.0	6.4	7.8	7.8
Housing	4.2	5.5	9.1	13.0	18.4	18.4
Health	**5.8**	**12.2**	**16.0**	**16.0**	**17.5**	**17.5**
Tourism	0.6	0.9	1.9	1.4	1.6	1.6
Religious affair	1.3	1.4	1.9	0.8	1.0	1.0
Education	**29.3**	**45.3**	**50.8**	**58.0**	**69.0**	**115.2**
Social Protection	**2.3**	**2.3**	**2.7**	**3.3**	**3.4**	**3.4**
Total	361.2	440.0	504.6	697.1	867.2	818.2

Source: Ministry of Finance, 2009

Moreover, the education sector takes the lion's share of the central government expenditure allocated to social sectors. While the share of social protection has been constant in recent years, the percentage of health expenditure to the total central government expenditure has decreased in the last two consecutive years. By 2005, the percentage of social protection expenditure was the highest in the 2005-2009 period mainly because of significant compensation programmes in 2005. Compensation programmes were aimed at mitigating the impact of fuel subsidy reduction on the poor. Some of these programmes are temporary in nature, and apply only when the government reduces fuel subsidy.

One of the temporary compensation programmes is *Bantuan Langsung Tunai* (non conditional cash transfer or so-called BLT). In 2005, two-time fuel subsidy reductions led to a dramatic increase in domes-

[13] This table is the breakdown of the central government expenditure on Table 2. The budget on Table 3 includes personnel expenditures, goods and capital expenditures, subsidies and social supports which are categorized into 11 functions above.

tic fuel prices, increasing by almost 150%. To mitigate their adverse impact, the government introduced BLT for 19.1 million poor households. Since then, BLT programmes were no longer carried out. However, BLT was reintroduced in 2008 due to the third fuel subsidy reduction. The beneficiary of BLT programme in 2008 was relatively the same as those in 2005. As the 2008 government spending also increased—in percentage of total central government expenditure—the percentage of expenditure allocated to social protection in 2008 was not as significant as the programme in 2005.

The allocated resource to the education sector jumped significantly in terms of percentage to GDP. In the 2008 proposed budget, the central government expenditure on education was 1.2% of GDP. By 2009, it has increased to 2.2% of GDP. Meanwhile, two other social sectors remain less than 1% of GDP for the last five years (around 0.3% of GDP in health and 0.1% of GDP in social protection). With that figure, it seems that there is no significant measure to address the vulnerability or poverty due to the financial crisis in 2009. Yet this may be the case because of the perceived limited impact of the current financial crisis on poor people.

Table 5. The Percentage of Central Government Expenditure by Function (%)

Sector	2005	2006	2007	2008 Proposed Budget	2009 Proposed Budget	2009 Revised Budget
Public Services	70.8	64.4	62.6	74.3	76.1	69.1
Defence	6.0	5.6	6.1	1.5	1.6	1.7
Home Security	4.3	5.4	5.6	1.8	1.8	1.9
Economy	6.5	8.7	8.4	8.2	6.8	7.2
Environment	0.4	0.6	1.0	0.9	0.9	1.0
Housing	1.2	1.2	1.8	1.9	2.1	2.3
Health	1.6	2.8	3.2	2.3	2.0	2.1
Tourism	0.2	0.2	0.4	0.2	0.2	0.2
Religious affair	0.4	0.3	0.4	0.1	0.1	0.1

Education	8.1	10.3	10.1	8.3	8.0	14.1
Social Protection	0.6	0.5	0.5	0.5	0.4	0.4
Total	100.0	100.0	100.0	100.0	100.0	100.0

Source: Ministry of Finance, 2009

Table 8. the Percentage of Central Government Expenditure to GDP

Sector	2005	2006	2007	2008 Proposed Budget	2009 Proposed Budget	2009 Revised Budget
Public Services	9.2	8.5	8.0	11.1	12.5	10.7
Defence	0.8	0.7	0.8	0.2	0.3	0.3
Home Security	0.6	0.7	0.7	0.3	0.3	0.3
Economy	0.8	1.1	1.1	1.2	1.1	1.1
Environment	0.0	0.1	0.1	0.1	0.1	0.1
Housing	0.2	0.2	0.2	0.3	0.3	0.3
Health	0.2	0.4	0.4	0.3	0.3	0.3
Tourism	0.0	0.0	0.0	0.0	0.0	0.0
Religious affair	0.0	0.0	0.0	0.0	0.0	0.0
Education	1.1	1.4	1.3	1.2	1.3	2.2
Social Protection	0.1	0.1	0.1	0.1	0.1	0.1
Total	13.0	13.2	12.8	14.9	16.4	15.5

Source: Ministry of Finance, 2009

Finally, poor budget documentation at the local government level makes the compilation of total government expenditures rather difficult. Many local government documentations are not made public.

CONCLUSION

The socio-economic impacts of the current global crisis have been contained in many ways, although some studies found that the crisis has severely affected the externally oriented sectors, such as manufacturing industry. A study by the World Bank (2009) estimated that several regions would be the most hard-hit by the current crisis. These regions' economies rely heavily on plantation crops (North Sumatera,

Riau, Lampung, and South Sulawesi) and on manufacturing industries (Banten, Jakarta, and West Java).

Nevertheless, recent data unwind our concern about employment and poverty. Data on employment show that the crisis has no significant effect on unemployment rates. At the same time, the performance of the labour market, as indicated by the percentage of formal workers, has been relatively stable in the 2008-2009 period. In fact, employment levels in the financial and manufacturing sectors grow steadily. Although such correlation between employment and poverty is a complex one, robust findings on employment data might suggest a relatively low impact of the current economic crisis on the poverty level. Unfortunately, reliable and indicative data are not available yet.

Judging from the impacts of the 1997/1998 economic crisis on education, predictably the current crisis would not lower school enrollment rates, particularly at the secondary level. Indeed, enrollment rates for the last two years have been stable. Concerning the health sector, as indicated by consumption level, apparently Indonesian households have changed their consumption pattern toward consuming more nutritious food. This is caused by an increase in purchasing power due to stable rice prices during the last three years. Therefore, concern over health deterioration due to declining quality of food consumption should not be a major issue.

Having learned from the previous crisis in 1997/98, the government decided to take a prompt action before the early impacts started to pinch in. They managed to avoid the sudden meltdown as experienced in 1998. Unlike in 1998, the government decided to expand its budget to encounter the economic slowdown. Fiscal stimulus package was designed to maintain domestic purchasing power[14] as private consumption was the prime mover of the economy—due to its sizable proportion in the country's GDP.

At the core of the fiscal stimulus issue was the concern over the proportion and effectiveness of (central and local) the package. A very sizable portion of the package was designed for tax reduction which

[14] In addition, there are some factors that might preserve domestic purchasing power, such as low commodity prices on the international market, good seasonal weather and the fact that 2009 was election year in Indonesia, where electoral (both legislative and presidential) candidates spend money on their campaigns.

may or may not affect private consumption since taxpayers—especially the middle class, may choose to save. The other concern related to the ability of both local and central government to quickly disburse the money. Should the government decide to continue these stimulus in 2010, complicated procurement processes and administration practices should be simplified and become more transparent than the procedures currently applied.

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REFLECTIONS ON THE POLITICAL ECONOMY OF POLICY REFORM IN INDONESIA

Hal Hill and *Chris Manning*

INTRODUCTION

Economists broadly agree on many key economic policy issues, but economics as a discipline has provided much less guidance on why and how economic policy reform occurs, and how to develop institutional mechanisms that enable governments to adopt 'good' economic policy. Political scientists are adept at identifying coalitions, constituencies, institutions and interest groups, but they less commonly examine the implications for economic policy. Thus, work at the intersection between economics and politics, of why and how policy reform takes place, remains relatively unexplored territory. This is especially so in developing countries: political processes are more personalistic, institutions are often less well established, outcomes more fluid, and the detailed case study literature on economic policy making is in its infancy.

The literature on the political economy of reform draws attention to the interplay of 'ideas, interests, and institutions', in the words of Bhagwati (2002). That is, ideas provide analytical content for political leadership intent on accelerating economic development, interests refer to the contending actors involved in the process of economic re-

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form, while formal and informal institutions shape the speed and success with which reforms can be implemented.

Other factors obviously affect the process. One is the 'crisis hypothesis', enunciated for example by Lal and Myint (1996, 288), that '[t]urning points [ie, major policy changes] are invariably associated with macroeconomic crises.' It is argued that reform is a difficult process, and societies have a natural ('Olsonian') tendency to become sclerotic. A crisis may be helpful in persuading the community that the current order is unacceptable and requires change. Political leadership may be emboldened, and willing to tackle difficult issues. In a very different political context, Bardhan (1998) draws attention to the relevance of this factor in India's reforms. The vested interests that built up around the post-independence dirigiste regimes, both financial and ideological, were formidable. But a fiscal crisis played a role as trigger in 1991, and economists (mainly expatriate academics) had played a powerful role in articulating a reform agenda. Externally, the collapse of the Soviet Union and the success of the Chinese reforms meant that the 'left had nowhere to go'. Obviously, however, this thesis does not have universal applicability.

There are many cases where crises result in failed states, or at least an inability to seize the opportunity to reform. That is, the hypothesis only works in certain circumstances.

A range of external actors and factors may make a difference. Two have already been identified. One is crises, some of which are exogenous (in the form of negative external shocks) and which have unpredictable effects. The second is ideas, many of which originate from abroad. For example, the intellectual ascendancy of openness as an engine of economic progress is highlighted in several country studies of trade liberalization (Rajapatirana *et. al.* 1997). More generally, a diverse set of foreign influences inevitably shapes the process. There is the demonstration effect of successful reforming economies, especially if they are located nearby. This is the notion of 'competitive liberalization' sometimes articulated by Indonesia's Trade Minister, Professor Mari Pangestu, and others.

The evidence on donor (particularly IMF and World Bank) conditionality is mixed. International agencies can play an effective role if there is a domestic interest in, and will for, reform (Krueger and Rajap-

atirana 1999). However, in the absence of these factors, externally-mandated reform attracts domestic opprobrium, implementation is likely to be spasmodic, and the reforms are therefore generally not durable. The 'revolving door' syndrome, highlighted in the African case especially by Collier (2007), illustrates the limited role for donors. These arguments are also consistent with the cross-country econometric evidence that finds aid contributes to growth only when 'good policies' are present.

The more successful reforms are invariably comprehensive. Political constraints may in reality result in piece-meal reform. But the danger is that significant gaps in the reform agenda may undermine the entire process. The literature on the interaction between macroeconomic and trade policy illustrates this issue, and also provides an intellectual rationale for the sequencing of reforms. As most analyses of successful trade liberalization point out, a willingness to allow a large depreciation boosts the competitiveness of tradable goods industries, and facilitates a lowering of protection. Krueger (1978, 231) for example argues that the '...failure to devalue by a sufficient margin will prevent sustained liberalization'; moreover, a '... realistic real exchange rate [is] an essential condition for sustained liberalization.'

Reforming comprehensively and quickly is also emphasized in the literature on the successful Chilean reforms. As one of the policy reformers concludes: 'It is no use freeing trade and opening up the capital markets if one is going to leave the labor markets untouched.' (Pinera 1994, 228) But he also underlines the need for judgement, and that moving decisively does not necessarily mean 'big bang'. For example, rapid macroeconomic stabilization is essential. Trade reform needs to move quite quickly, perhaps over a five-year timetable, long enough to allow economic agents to adjust, but not so long as to allow opposition to build up. Tax reform is a more complex matter, and will take a longer time to formulate and implement.

The bureaucracy is typically not a significant player in the formulation of major reform programmes, but it may be a critical player in implementation. The general presumption is that the bureaucracy is a reluctant reformer to the extent that reform entails a loss of privileges. However, much depends on:

- the relative strengths of the executive and the bureaucracy, and the institutional independence of the latter. If, as in the Philippines, senior echelons of the bureaucracy turn over with each administration, the executive is generally able to operate with little bureaucratic resistance;
- the relative strength of reform-minded sections of bureaucracy, in particular the areas of analytical strength such as ministries of finance and central banks;
- the nature of reform. Programmemes of deregulation—e.g,, replacing a central bank with a currency board, bypassing a corrupt customs service—by definition do not require bureaucratic implementation. But complex programmemes, such as tax reform and decentralisation, do require active bureaucratic cooperation. And establishing new institutions, such as a revamped judiciary, can be extremely complex, long-term projects.

Finally, political leadership is essential. This may take many forms, and will obviously depend on the nature of the political system. In authoritarian regimes, where power is heavily concentrated around a key political figure, such as Soeharto's Indonesia or Pinochet's Chile, reform may proceed very quickly once that leader is persuaded of the case for reform. Democracies may also reform successfully, of course, but the process is typically slower, and involves developing broader coalitions of support. Reforms are obviously more likely to be durable the more institutionally embedded they are, and the less they depend on a particular individual.

Autocratic systems of government, like that of Soeharto, have the means to implement far-reaching economic reforms, through the controls they exert over the political system. However, an abrupt transition to a democratic regime, as occurred in Indonesia in 1998–1999, has the potential to disturb many of the conditions which underpin economic expansion under a pro-growth autocratic government. This is especially true where the changes required to sustain growth threaten the livelihoods and economic standing of interest groups, or significant sections of the wider community. New democratic governments can find it difficult to stick to a consistent reform programme, especially if

the President loses control over the legislature, and key economic portfolios are held by coalition partners with different policy priorities.

THE INDONESIAN EXPERIENCE: GENERAL CONSIDERATIONS

A brief survey of the political economy context during the New Order and in the post-Soeharto era provides a background to our discussion of the four episodes of reform. Especially in the first two decades of the New Order, Indonesia under Soeharto had many of the features of an autocratic government committed to economic progress (Bresnan 1994; Hill 2000). The close working relationship between the President and the tightly knit group of technocrats who controlled economic portfolios was a key feature of the regime. It enabled the passage of economic reforms which stabilized the economy, and promoted agricultural development, population control, trade expansion and foreign investment. Soeharto's trust in the technocrats also helped Indonesia deal with periodic economic crises, especially in the early years of the regime (Hoffman et. al. 2007). The widely documented control over the electoral process, political parties, the legislature, the media and other potential opposition groups enabled the government to press forward with its sometimes unpopular economic agenda without significant challenge.[2]

However, when it came to explicit support for market-oriented economic policies, Soeharto was no Pinochet. Nor were the 'Berkeley mafia' of US-trained technocrats who advised him as doctrinaire as the 'Chicago boys' who managed the Chilean reforms (Pinera 1994). While the government initiated a raft of reforms in the area of trade, as noted above, neither Soeharto nor his technocrats demonstrated a strong ideological commitment to market solutions.[3] A preference for cooperatives and protective government labour regulations were a reflection of a strong paternalistic streak and ambivalence with regard to market solutions (Soeharto 1989: 233). But, at the same time, the technocrats had experienced the political and economic costs of high levels of government intervention in the economy under Soekarno. They also understood that Indonesia as a potential commodity exporter stood to lose heavily from isolating itself from international markets.

The institutional environment changed dramatically with the breathtaking pace of political reform after the fall of Soeharto: the first

free elections in 1999, 'big bang' decentralisation in 2001, constitutional reform in 2002, the first direct Presidential elections in 2004 and progressive elections for district and provincial governments over the subsequent three years. After the initial three years of frenetic political change and sometimes chaotic economic policy-making, several key patterns had emerged by the mid-term of the Yudhoyono presidency. The power of the Presidency and executive was weakened, and that of the legislature strengthened.[4] Economic portfolio cabinet ministers now were obliged to negotiate most major regulatory changes in the parliament.

Major pieces of legislation, such as revisions to the tax and investment laws, all took at least twelve months and often much longer to gain parliamentary approval. Second, ministers appointed in successive coalition governments no longer spoke with a single voice, nor did their ministries pursue a consistent line on economic policy, in contrast to decision-making during much of the Soeharto era. Cabinets now consisted of broadly-based multi-party coalitions, and different policy agendas emerged, for example between the Finance and Trade and Industry Ministers over trade policy under Megawati, and between the Ministers of Agriculture and Industry and the Ministers in the key economic portfolios—Finance, Trade and the Coordinating Minister of Economic Affairs—on protection for industry policy (Awiscahyono and Hill 2004; Basri and Patunru 2006).

In addition, interest groups, including business and labour unions and groups ostensibly representing the interests of farmers, such as the Farmers Association, HKTI, led by ex-military leaders, had much more access to decision makers in the parliament and the bureaucracy, and the media. They also had greater access to cabinet ministers in rainbow cabinets who were no longer protected by, or directly answerable to, a powerful President. In addition, there was now constant public scrutiny of government performance from civil society groups and the media. Freedom of the press, in particular, was important in putting pressure on the government to reform social policy.

Two other features of the policy-making environment are also relevant for policy-making in the *reformasi* era. First, the media, many parliamentarians and some cabinet ministers adopted a more nationalistic stance regarding openness to the world economy, including foreign

investment in certain sectors (such as mining). They were also critical of international financial institutions (IFIs), such as the IMF and World Bank. The economic crisis had dented Indonesian policy-makers' confidence in IFIs, not least for their strong advocacy of market solutions that rested uneasily with many of the political elite when Indonesia was on its knees during the financial crisis (Johnson 1998; Robison and Hadiz 2004, 148-149).

Second, the resentment about corruption, cronyism and human rights abuses that had built up under Soeharto now meant that the achievements of his government were accorded less credit in public discourse and the political arena. Besides the well known economic 'miracle', these accomplishments were in areas such as employment growth, stable rice prices and poverty alleviation. The latter set of issues, of fundamental importance to the poor, was much less in the political spotlight than corruption cases involving high office bearers in the political and bureaucratic arenas. Galvanizing public support for 'neo-liberal' economic reforms in areas such as trade reform, privatization, or labour, was likely to prove a difficult task for the new post-New Order governments, precisely because of a widespread, popular but mistaken belief that the Soeharto regime's 'neo-liberal' economic policies under the guidance of the IFIs had not significantly benefited the poor.

THE INDONESIAN EXPERIENCE: CASE STUDIES

Since there is no 'one size fits all' conclusion to this international literature, we now investigate some Indonesian reform episodes and policy challenges, and ask how closely they conform to the hypotheses generated from the international literature referred to above. Our survey briefly considers four areas of policy-making processes and outcomes: trade reform, privatisation and SOE (State-Owned Enterprise) reform, labour market intervention and rice policy. The first two of these case studies each deals with an area of policy success (trade reform) and an area of disappointment (privatisation) over several decades. In the third and fourth cases, labour and rice, we examine how the process of policy formulation and reform was transformed, and became more complex, after regime change from an autocratic to a more democratic system of government in Indonesia in 1998.

Trade Reform

Indonesia achieved comprehensive reform in the mid-1980s, which elevated growth rates and almost certainly averted a serious debt crisis. As oil prices began to decline sharply in the early 1980s, the government's macroeconomic response was prompt and effective, combining fiscal prudence, exchange rate depreciation and monetary policy caution, supported at that time (unlike in 1997–98) by a helpful international donor community. Once macroeconomic stabilisation was secured, the government turned to microeconomic measures, and implemented a comprehensive reform package. In trade policy, most NTBs were gradually removed, and tariffs lowered and unified. Exporters were placed on a free-trade footing through an effective duty exemption and rebate system. A sweeping reform of customs sidelined the deeply corrupt and obstructive import/export procedures. Foreign investment restrictions were relaxed. The financial sector was deregulated and the stock market reactivated. Many regulatory barriers to entry were removed, particularly in sectors formerly dominated by SOEs, such as the strategically important inter-island shipping industry.

What explains the success of these reforms?[5] As most analysts of this episode note, strong opposition to the reforms was to be expected. The dominant ideological predisposition of the influential policy community was suspicious of liberalism. As soon as the macroeconomic stabilisation and liberalisation of the late 1960s began to bear fruit, the pendulum swung back towards dirigisme and control, reinforced by the huge commodity windfall gains. As an indication of the sensitivities, whenever liberal reforms were introduced, they were always referred to by the neutral term 'deregulation'. Moreover, vested interests had built up around the complex system of controls and intervention, in the business sector, the SOEs and the bureaucracy. There was by contrast a weak export sector and a tiny, marginalised intellectual community calling for reforms.

Several factors were central to the success of the reforms, and these are broadly consistent with the formulations of the international literature on the subject. First, the reformers—that is, the so-called Berkeley Mafia—were respected, technically competent, had a clear sense of policy objectives and priorities, and they had occupied all the major economic policy portfolios since the beginning of the Soeharto

era. Second, although lacking any direct political support, they had developed close relations with Soeharto, who by then was the country's supreme leader and whose interests lay in the restoration of economic growth. The technocrats were thus able to persuade Soeharto of the reform imperative. Third, the reforms were comprehensive, effectively implemented, paid attention to equity dimensions, and began to produce results—particularly the spectacular growth in manufactured exports from the early 1980s—thus averting a looming debt crisis and restoring growth. A range of additional factors was also helpful. These included, in particular, the constructive support of the donors and IFIs, and the reform momentum throughout the entire East Asian region. The domestic opposition to reform was also quite tepid, with the likely sources, such as the bureaucracy and economic nationalists either silenced or co-opted. It is important to emphasise that the Soeharto family business empires were then in their infancy, and that these interests therefore could not sabotage the reform agenda in the manner that they were later to do at the time of the 1997–98 crisis.

More generally, looking at the specifics of trade policy reform during the Soeharto era, Basri and Hill (2004), drawing heavily on Basri (2001), explain these trade policy dynamics with reference to changes in the relative influence of several key policy actors over this period. That is, they identify the key policy actors, their general trade policy preferences, and how influential they were during each major episode of the Soeharto period. These actors include the technocrats, economic nationalists, 'rent seekers' more generally, and donors and foreign advisers.

Thus the drift towards increased protection in the 1970s occurred because both the technocrats and foreign influences on policy were on the wane, at least in the realm of microeconomic policy. They were less needed during these 'good times', and there was less imperative to follow their policy orthodoxy. Moreover, neither group was completely united on core trade policy issues. Economic nationalists were becoming increasingly powerful over this period, and were able to build opportunistic alliances with various rent-seekers. By contrast, in the mid 1980s, the opposition to trade liberalisation was on the wane. The technocrats were united and stronger in their resolve to reform and, at that time of looming crisis, they had the ear of Soeharto.

Foreign influences were becoming more clearly pro-reform, and they had more weight. Indonesia needed funding from the IFI's to help it adjust to lower oil prices. Foreign investors were becoming more interested in the country as a low-cost export platform or as part of internationally integrated manufacturing operations, rather than as a relatively small and protected domestic market. Neighbouring countries, most especially China, were liberalising and growing rapidly, in the process constituting a powerful demonstration effect. Finally, the idea of coordinated, open, region-wide liberalisation, in the form of both APEC and AFTA, was beginning to take root in elite government and business circles.

In retrospect, it might have been expected that these trade reforms would have been unwound in the wake of the 1997–98 crisis, given that crises sometimes cause governments to resort to protectionism, that these reforms were associated with the now tainted Soeharto regime, and given also the unpopularity of liberal economic policies in the wake of the crisis. Nevertheless, Indonesian has remained open, albeit precariously, since the crisis for a range of political economy reasons (see Bird *et. al.* 2008).

Privatization and SOE Reform

In contrast to the success in trade policy, state enterprise reform in Indonesia has proven to be much more difficult even during the high point of reform during the mid 1980s. Here too the literature on the political economy of reform facilitates our understanding of such an outcome.

The case for reform in this sector is a strong one. Most studies of SOE (state-owned enterprise/*Badan Usaha Milik Negara/BUMN*) performance report inferior commercial outcomes, both in strictly commercial terms and according to a broader range of non-commercial objectives imposed upon them. These performance indicators in any case need to be interpreted with caution, because they generally exclude both a range of implicit subsidies (e.g,, restraints on competition, favoured access to credit and government procurements, tax waivers), and exactions imposed upon them (e.g,, over-staffing, uneconomic location decisions). That is, these enterprises generally operate with multiple, sometimes conflicting, objectives. Perhaps most importantly, they are

irresistible vehicles of political patronage. The latter incidentally seems to be a feature of both authoritarian and democratic regimes.

Indonesia has traditionally had a large SOE sector, inherited from the pre-1965 nationalisations of foreign property, and boosted by large investments during the oil boom era, 1973–81. It is notable that there have been very few privatisations, even in the major reform episodes of the late 1960s and mid 1980s. In the latter case, arguably, the technocrats judged the 'political cost/benefit ratio' to be too high. That is, there was a big reform agenda elsewhere—in trade, investment, tax, finance—that they judged could be enacted with less cost and perhaps greater benefit. They therefore adopted indirect approaches to the reform of SOEs.

Why has SOE reform been so difficult? The main factor has been the strength of opposition. First, bureaucrats in the line ministries have regarded them as a convenient instrument of patronage. Senior officials sit on the boards of SOEs under their purview, either concurrently with a salary supplementation or upon retirement, or both. Second, local opposition to the disposal of SOEs, both from the employees and the community, is generally strong. This arises in part because SOEs have often had a strategic locational component. That is, they have been established in regions as a means of boosting local development and vote buying. They therefore assume disproportionate importance in the local economy and its politics. This was a consideration in one of the most high-profile privatisation failures in Indonesia, involving the attempt by Cemex (ironically a foreign investor from the 'South') to purchase a large SOE cement company (Prasetiantono 2004).

Third, privatisation programmes have been particularly vulnerable to xenophobic sentiment and to considerations of ethnic balance. This is a potent factor: to the extent that the buyers are foreign or ethnic Chinese, those with a vested or ideological interest in maintaining a large SOE sector are able to whip up strong community sentiment opposing the sales.

Paradoxically, trade liberalization might be thought to go hand in hand with privatisation, but often the reverse is the case. This is because SOEs are seen to be the only remaining bulwark against competition from both domestic 'conglomerates' and imports.

An additional concern is that, if the reformers cannot control the privatisation process, it may be preferable not to proceed. This has been a consideration in Indonesia. In the late Soeharto period, reformers began to oppose the process of privatisation on the grounds that it had become 'familization', as members of the Soeharto family bought up state assets. In Malaysia, the process of disposing of SOE assets at sub-commercial values to selected political patrons—in this case the well-connected in the Bumiputera community—has proceeded much further (Gomez and Jomo 1997).

Where outright sale has proven to be too difficult, reformers have had to resort to useful but second-best options. Two in particular have been employed. The first is to deregulate the sectors dominated by SOEs, and ensure they face competition. In Indonesia, for example, this has occurred effectively in civil aviation, banking, telecommunications and domestic shipping. These were all formerly exclusive or dominant SOE sectors. Deregulation produced a strong private sector response, and it eroded SOE rents. The second strategy has been to impose a hard budget constraint on SOEs, both directly in the form of government resources and indirectly through curbs on borrowing from the banking sector. An additional variant has been to record all transfers from the government budget to SOEs, to publicise the costs of these subsidies.

These second best measures arose because the reformers made a strategic calculation that they did not have the political authority to privatise cleanly, but they did have enough power to enforce greater competition. The reforms invariably originate from the Ministry of Finance, which is generally the only pro-reform agent within government on this issue.

Labour Policies[6]

Partly related to the trade reforms achieved under Soeharto that we have described above, the number of jobs grew rapidly, wages rose in the export-oriented industries and poverty declined in the decade leading up to the crisis in 1998 (Manning 1998). This occurred in the context of a quite flexible labour market, where the rights of trade unions were tightly controlled by a military regime concerned with security and political stability (Hadiz 1997). Thus despite the achieve-

ment of jobs growth and associated poverty decline, many commentators saw the denial of labour freedoms in the New Order period as 'the' labour problem. Understandably, they welcomed the new, more democratic regime of the successive *reformasi* governments that offered trade union freedoms and greater labour protection (e.g., Lindsay and Masduki 2002; Caraway 2006).

Indonesia is not unique in seeking to deal with the potential conflict between a focus on economic growth which provides jobs for the poor, on the one hand, and the potential cost in terms of employment and mass living standards of greater freedoms after political transformation, on the other (Haggard 2000; Cox-Edwards 1997). In the case of Indonesia, labour has been one area where democratic governments after *reformasi* have adopted a major reform agenda. One priority was the reinstatement establishing basic labour rights through ratification of ILO conventions and the passing of the Trade Union Law No.21/2000, which sought to guarantee rights to organise and bargain collectively.

In contrast to Soeharto's 'security first' approach, several former trade unionists were appointed as Ministers of Manpower in post-Soeharto governments. These appointments were symptomatic of a major shift in government policy towards greater support of labour rights and standards. Improved standards were promoted by an aggressive and comprehensive minimum wage policy and the all embracing government Law No. 13 on Labour Protection passed in 2003. In addition to seeking to guarantee a wide range of rights and basic working standards, the Law legislated for much higher rates of severance and tighter controls over contract workers than in the Soeharto era (Manning and Roesad 2007).

A key issue was the impact of all these changes on the welfare of wage workers and employment. Formal sector employment growth had been much slower in Indonesia in the post-Soeharto era, and many policy makers were concerned that this slowed the rate of poverty decline (Manning 2008). Some officials in Bappenas made consistent public representations for more laws which allowed greater flexibility in wage setting, and hence supported job creation. Nevertheless, it appears that the political odds were strongly stacked against winding back some of the clauses in the 2003 Manpower Act which threatened employment creation.

Difficulties in reconciling the labour reform agenda with the urgent need to promote investment and jobs were particularly stark in the case of policies adopted by the government under Soesilo Bambang Yudhoyono (SBY) (2004–2009). SBY set ambitious targets for creating jobs and halving unemployment as one of the main goals of his government. To do this, his government needed to address some of these more restrictive aspects of the labour law. As a result, the Ministry of Manpower made recommendations during discussions with unions and employers in February 2006 for significant revisions to some of the more controversial clauses of the Manpower Law No. 13/2003.[7]

Revisions to the labour legislation were subsequently incorporated together with other proposed legislative changes (including the tax, customs and investment laws) in the Economics Coordinating Minister's plans to improve the investment climate (Indonesia Coordinating Ministry for Economic Affairs 2006). The World Bank in particular had provided strong public support of reforms in all these areas during 2005, including co-hosting a major international conference in cooperation with the Indonesian Chamber of Commerce (KADIN) and opened by the Vice-President, Jusuf Kalla, in November of that year (World Bank 2005).

The proposed reforms met with stiff opposition. All the major union confederations rejected the proposed changes to the labour law out of hand, partly because they felt that they were not sufficiently engaged in drafting the original draft proposal. The government was faced with increasingly vocal opposition, culminating in major demonstrations in Jakarta and in several other cities in April and May 2006.[8]

Although the show of opposition was not particularly large by international standards, President Yudhoyono announced quickly in May that proposed revisions to the labour law were to be withdrawn from the national economic reform package, only several months after they had begun to be debated in the public domain. As a face saving device, the President appointed a 'Five University' team of experts to examine options for labour reform. However, it is widely acknowledged that any significant revisions to the labour law were too 'hot' politically and off the government reform agenda at least until after the elections of 2009.

The failure of attempts to revise a pro-labour law is a clear case of populist politics dominating pragmatic economic policy that sought to create more jobs and improve welfare among working people. One issue was fear of a union and wider community backlash against any reforms which appeared to be against the interests of labour, in this case represented mainly by wage workers in the modern sector. Reforms aimed at reducing hiring costs and rigidity in employment and wages were too sensitive a subject for political leaders. The case demonstrates the potential role of political leadership (or absence of) in championing reform. Although his Vice-President strongly supported the reforms, SBY was not prepared to risk popularity through backing labour reform. None of the major political parties publicly supported winding back restrictive clauses in the labour law, or sided with business in its attempts to modify the severance pay and minimum wage regulations.

Ideology was also important in this case. Paternalism persisted as part and parcel of the labour regime inherited from Soeharto, who had extended government protection for workers in the form of minimum wages and other benefits to compensate labour for the lack of collective rights and freedoms in the late New Order period. Despite the removal of the restrictions on labour freedoms and rights to bargain collectively, and the emergence of an active trade union movement, there still existed a common belief that far-reaching government regulation was necessary to protect workers from rapacious employers, even in the post-Soeharto era. Like the term 'economic liberalisation', 'labour market flexibility' was viewed negatively by many civil society groups including labour unions.

Rice Policy

As noted above, President Soeharto and the technocrats understood the paramount importance of low food prices for the poor, as well as the political importance of stable and low rice prices for the urban middle class. Even though rice self sufficiency was a major goal of the New Order regime, tight political controls meant that governments were never hostage to the food producer lobby, which has been so important in many developed and developing countries internationally (World Bank 2007). Democratisation changed the political dynamics

of rice policy, however. Farmer groups (or politicians ostensibly representing them) were now in a position to lobby government in the interest of more concentrated producer groups. Civil society groups and political parties also raised the issue of trade in rice as a nationalist issue in the media and the parliament. In our discussion of the political economy of rice policy we look briefly at the balance of interests in rice production and prices, and the evolution of rice policy during the New Order and the *reformasi* period.

Rice is Indonesia's single most important commodity for consumption, employment and welfare, especially among some five million poor households whose total expenditure is below the national poverty line. Rice prices, production and policies are thus big public policy issues in Indonesia. The balance of producer and consumer interests is complicated, however. Most farmers (two-thirds) and a significant number of rice farmers (around 25%) are net consumers rather than net producers of rice (McCulloch 2008, 54). Thus although rice accounts for around two-thirds of the total harvested area to food crops, many rice farmers have an interest in low prices and deregulated international trade in rice, which should help to keep prices low. As might be expected, this includes many among the poor, including a significant number of poorer rice farmers, *petani gurem*, who operate less than 0.5 hectares, mostly insufficient land to produce enough rice to feed their families.

Nevertheless, there is a significant group of farmers who are net producers of rice and stand to gain from high rice prices—probably around one million household heads. Although almost all these farmers own small amounts of land by international standards, this is a potentially large pressure group by any standards. Better-off producer households are, moreover, relatively concentrated in a few regions: the better irrigated areas of lowland Java and Bali and in certain *kabupaten* (regency) in South Sulawesi and Lampung.

However, these producer interests need to be balanced against those of consumers. From the point of view of consumers, low rice prices are significant for living standards of many Indonesians. Rice has accounted for 15% of all consumption among Indonesian households and 25% of total expenditure among the poor in recent years (McCulloch 2008). In this respect, Indonesia is unlike many other high-

er income Asian countries where food and rice consumption make up a small proportion of total expenditure, and where the political economy of rice is tilted in favour of protection of producers rather than lower prices for rice consumers (World Bank 2007). Thus any general rise in rice prices is bound to cause a political stir, as it did during the last years of Soekarno's rule and at several times early in the New Order period.

What have been the main government policies to meet the competing interests of consumers and producers of rice, and how have these changed with the transition to a more democratic government? Given the importance of rice for the daily consumption of average Indonesians, rice self sufficiency has been a goal articulated by all governments since independence. But only for a brief period in the country's modern history was this goal attainable, during and in the immediate aftermath of the oil boom period of the 1970s and 1980s, when very substantial resources could be devoted to rice production (Manning 1987). At the same time, during most of the New Order period the government allowed periodic imports to augment a national buffer stock, thus ensuring that domestic rice prices were kept more or less in line with international prices (Timmer 1996). In general, the policy was successful. A delicate balance was struck between meeting the interests of producers through expanding production, on the one hand, and the interests of consumers by maintaining low and stable prices, on the other.[9]

A number of conditions which underpinned the successful rice policy under the New Order began to unravel in the post-Soeharto period. Limited resources, decentralisation and a more nationalistic stance fed by interest group pressures meant that it was more difficult to maintain this balance between producer and consumer interests. Production growth was slow. The government no longer had the resources to promote rice production and decentralisation has contributed to public underinvestment in agriculture (Simatupang and Timmer 2008).

After stabilising in the wake of the 1998 crisis, rice prices were relatively steady for a period when private traders were allowed to import rice. But from 2004 onwards there was growing opposition to the market-oriented policies in rice trade that had been promoted by

the IFIs. This was signaled by the appointment of a more nationalistic Minister of Agriculture from a minority party in government. Bulog was reinstated as the sole rice importing agency and the government banned rice imports, only permitting them when the rise in domestic prices threatened to create political unrest.[10] Now under the ambitious former son-in-law of the former President Soeharto, Prabowo Subianto, the Farmer's Association appears to have played a role in influencing public opinion through periodic statements in opposition to rice imports. Finally, unlike in the New Order period when the President played a decisive role in guiding policy, from 2004 SBY failed to give clear direction in policy, not least through his appointments of a protectionist Minister of Agriculture alongside more market oriented Ministers of Trade and Finance who were responsible for tariff and trade policies.

CONCLUSION

Three main conclusions emerge from our examination of the Indonesian experience of the political economy of public policy and reform. First, while there were some common lessons in the evolution of public policy in the four areas examined in this paper, we are struck by the differences related to specific interplay of ideas, institutions, interests and political and bureaucratic actors in each of the case studies. Common themes especially relate to the tension between advocacy of more market oriented ideas generated in the international arenas, often sponsored by the IFIs, and deep nationalist and populist sentiment. The latter is frequently stirred on some issues for sectional advantage and subsequently championed by the media.

Differences relate to the perceived benefits from reform and the different degrees of difficulty of reform in specific areas, partly related to the political influence of vested interests, and the extent to which the reforms could be easily caught up in debates on sensitive nationalist issues. In the case of trade reform, tangible benefits can be felt quite quickly, in contrast to longer term gains from SOE and labour reform. Privatisation is an area where interest groups are particularly strong, whereas labour law reform and removal of rice import bans strike a chord with politicians and parties looking for populist issues that will improve their electoral prospects.

Second, of all the factors discussed as important for the political economy of reform, we rate leadership very highly. In all cases of reform discussed above, it was Presidential support or lack of support for reform that played a decisive role. In particular, reforms involving complex distributive outcomes require strong support from the President. This appears to have been true both under Soeharto and in the *reformasi* period, although policy makers needed to mobilise the support of a much wider coalition of partners in the latter case. However, we note that bureaucratic obstacles do not seem to have played a major role in Indonesian reform episodes compared with some other countries.

Third, our case studies also demonstrate that given the right preconditions, reform can be undertaken more quickly and can be more comprehensive in a more autocratic rather than a more democratic system of government. Especially in a new democratic system, where parties appeal on the basis of broad and often shifting principles, rather than clearly defined policies, interest groups are often able to mobilise demonstrations of support through the mass media and thus convince political actors to back their cause.

Thus our case studies suggest that policies aimed at creating a more competitive economic environment, in particular, are likely to be more difficult for Presidents and coalition governments in a more democratic environment. In the case of Indonesia, part of the explanation relates to perceptions. Soeharto is considered to have been too pro-market and too pro-business by many political activists. Furthermore, in the post-Soeharto era there is greater suspicion of engagement in the world economy. After the initial economic reforms were imposed on Indonesia by the IFIs (International Financial Institution), out of necessity immediately after the crisis, the market-oriented reforms of *reformasi* governments have needed to be much more cautious, and more mindful of potential nationalist and populist backlashes. One lesson is that rushed reform agendas imposed in times of crisis may not have much staying power, especially if the benefits are not immediately obvious. The mobilisation of broad coalitions may contribute to more enduring reforms, even though there is often more noise than action in a more democratic system.

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THE NEED TO REFORM POLITICAL AND ECONOMIC INSTITUTIONS IN INDONESIA

Maria Monica Wihardja

INTRODUCTION

There is a strong reason why Indonesia should think seriously about reforming her domestic institutions. What is meant by domestic institutions here is not only explicit and implicit rules with some enforcements as defined by North (1990), but more specifically it is defined as a system consisting of rules, organizations or stakeholders, beliefs, norms, and the implied behaviours of the organizations or stakeholders (Greif, 2006). This system needs to be in equilibrium. Reforming rules without giving the incentives of the stakeholders to follow those rules will not make the rules work for what they are intended to create. They might in fact work against those intentions.

So, what we refer to as institutions are "rules that work" and not merely rules as what many people would have interpreted. Examples of institutions in Indonesia include local or district-level regulations, behind-the-border trading regulations, financial regulations or banking supervisions, and legal as well as judicial systems. Why are institutions important and why should enhancing institutions be our priority among other seemingly important economic agendas?

"Indonesian people live by 'the rules of the jungle'. Whoever is the strongest wins." This is an expression to describe the poor quality, if not the non-existent, of Indonesian institutions. What we have is

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mostly relation-based institutions, instead of rule-based institutions. Dixit (2004) argues that although relation-based institutions could sustain economic growth in small economic activities through localization of information and honesty, it is not sustainable after some level of development because of constraints on communication technology.

Because of this, middle-income countries, such as Indonesia, might be trapped in a situation in which relationship-based institutions no longer work, but the size of the economic activities or the level of development is not big enough to afford a rule-based institution. Whether or not there have been significant improvements in this perspective in Indonesia, the process from the relation-based towards rule-based institutions is still not complete and sufficient to support the growing economic activities. This is evident by the continuous distortions in economic sectors because of corrupt legal and judicial systems, for example.

We are going to look the need to reforms institutions in Indonesia from three angles: politics, economic, and international relation.

POLITICAL INSTITUTIONS IN DECENTRALIZED INDONESIA

It is not arguable that local or district-level regulations still need continued supervisions from independent watchdogs such as the Corruption Eradication Commission (*Komisi Pemberantasan Korupsi*/KPK). Huge autonomy given to local leaders is not balanced by the reward-and-punishment system in Indonesia. This is exacerbated by politically uninformed, uneducated, poor citizens in many districts in Indonesia that further constrain local accountability. Local direct elections have also given rise to local capture in which local elites support political candidates in returns for political favours during their leadership.

Based on the author's field study in five Indonesian districts in 2008, it was found out that KPK had been an effective corruption-deterrence body among public officials. When asked about corruption surrounding the local governments, many, if not most, interviewees said that there was no more corruption because of the emergence of KPK and it has effectively made the local bureaucrats fear to corrupt. Hence, KPK seemed to serve as a stick or punishment mechanism to local governments. Nevertheless, with the degrading popularity and existence of KPK, this stick or punishment mechanism is also dimin-

ishing with the dangers of increasing corruption at the local or district level.

With the weak, if not also corrupt, legal and judicial system in Indonesia, there is a little chance that decentralization will achieve its desired outcome. This brings us to the issue of the urgent need to reform Indonesian legal and judicial system both at the central and district levels. Many observers also argue that the decentralization in Indonesia is incomplete. Although local expenditure has been decentralized, local revenues have not been decentralized.

Regional development has been slowed down by central government policies such as in East Kalimantan where constraints on privatization of infrastructures inhibiting the region from developing to its full capacity. What is more important and debatable is whether decentralization actually "works" to achieve its goal namely enhancing people's welfare, or decentralization has aversely created "local kings" and "decentralized corruption". The evidence that decentralization works is very little as argued in Pepinsky and Wihardja (2009), Azis and Wihardja (2009), and many local fora conducted to celebrate the eighth anniversary of decentralization.

Take one indicator: poverty. As discussed in the eighth anniversary decentralization forum held by Bappenas, UNDP, and Kompas on 7 May 2009, there had been a very little change in poverty. Out of 33 provinces, only 18 provinces experienced an increase in poverty level, while the other 15 provinces experienced a decrease. Human Development Index has declined nationally. Moreover, 80% of the 205 new districts were considered failing (*Lembaga Ketahanan Nasional* 30 September 2009). Using a synthetic case control methodology, it is shown that decentralization has had no significant effect on Indonesia's economic output as measured by gross domestic product (Pepinsky and Wihardja 2009).

According to Azis and Wihardja (2008), high degree of local capture by local elites distorts the decentralization process. They also argue that the difficulty in reforming institutions in Indonesia lies on the endogeneity of institutions that could create a vicious cycle of low quality of institutions and low level of welfare. The policy implication of this paper includes the need of reward-and-punishment schemes to give incentives to local leaders to increase welfare.

MICROECONOMIC INSTITUTIONAL REFORMS

What have rescued Indonesia from the ripples and waves of the 2008 Global Financial Crisis are the strong balance sheets of Indonesian firms and banks, among other factors (Zavadjil 2009). The low public debt ratio of 33% and the deficit of .01% of GDP at the end of 2008 also provided a cushion for the government against crisis by allowing the government to provide necessary stimulus fiscal package. Foreign exchange reserves stand at above 200% of the short-term debts, which protect the Rupiah from speculative attacks and protect the capital from massive outflows.

Indonesian banks' capital adequacy ratio is around 17% compared to the 8% Basel II Accord requirement. Hence, this gives rooms for the government to increase public debts to build infrastructures and spend on other public expenditures, and for investors and consumers to take on more debts. However, as Zavadjil argues, the most difficult part is to provide a better legal and regulatory environment to implement this. Legal and regulatory environment in this sense includes financial regulations and banking supervisions as well as reforming the judicial system.

Strong macroeconomic indicators are necessary but not sufficient conditions for enhancing people's welfare. High poverty level, inequality, and unemployment rate remain to be unsolved for so many years, especially after the 1997 Asian Financial Crisis. Economic prosperity at the macroeconomic level does not seem to trickle down to the microeconomic level. It could be that the tight monetary policies, including the tight deficit that has rescued the macroeconomics stability, come at the cost of economic development, such as infrastructures, that could have given rise to employment and household incomes. Or it could be something else, such as structural issues. But, what is clear is that, despite a strong macroeconomic sector, Indonesia's microeconomic sector is still struggling. Parallel to Soesastro's "second-generation" economic reforms (Soesastro 2008), we need second-generation institutional reforms at the microeconomic level so that macroeconomic stability could have a meaning in terms of poverty, inequality, and unemployment. Examples of microeconomic institutional reforms are providing greater accesses to and qualities of education, health, and credit to the poor as well as reducing structural unemployment.

Increasing export competitiveness is not a neglected economic wisdom even in the era of re-balancing the global imbalance, in which surplus countries are expected to be less export-dependent. Petri (2009) had his point that we should not "throw the baby out with the bath water." We still need to remain increasingly competitive for our exports, increase efficiency in our manufacturing sectors, and tackle behind-the-borders trade barriers. Indonesia's export depends on volatile world market, such as mineral and agricultural commodities (ADB 2009).

Moreover, we have seen exports of textiles, electronics, footwear, pulp, paper, and wood products stagnated while the world market for these products increased. Logistical weaknesses in transportation, infrastructures and electricity become bottlenecks in Indonesia's trade. Inability and a lack of facilitation to mass-produce have hindered micro and small enterprises to export their products, and the loss is significant, according to the Ministry of Trade, Mari Elka Pangestu. Zavadjil (2009) further argues that credits remain difficult and inaccessible to much of the population because of problems in judicial systems. Microeconomic institutional reforms indeed need a lot of political commitments.

INDONESIA'S CONTRIBUTIONS TO THE GLOBAL AND REGIONAL INSTITUTIONS

Being part of the G20 is not a coincidence. Indonesia being the second largest democratic country, with the fourth largest population and the largest Muslim population as well as with many strategic commodities has the potential to become increasingly influential in the global governance. Together with Australia and Korea, Indonesia is a part of the middle-power countries (often is referred as "KIA"). It is neither as economically powerful as China nor Japan, but it is significant enough to influence the economy globally. Indonesia is also part of the ASEAN+3 (APT), which is consolidating its existence as a regional financial institution by creating a self-managed reserve pool worth US$120 billion on top of facilitating multilateral swaps. It has recently created a stepping stone towards operating the reserve pool and the multilateral swaps, which have not been operational, by establishing an independent surveillance body with the help of ASEAN and ADB secretariats.

Why the establishment of an independent surveillance body (or an independent peer-review, as opposed to a national peer-review) is important is because information plays a significant role in coordinating actions and in any financial transaction. Like any public good, information suffers from a collective action problem, namely, no country self-interestedly seek to reveal their information, although information revelation by all will make all countries better off. Hence, information is a very important institutional element in coordinating within a regional or global institution.

According to the Dincer and Eichengreen Index on transparency of Central Bank, from 1998 to 2005, Indonesia is considered a moderately transparent country among the APT countries. There are two periods when Indonesia made a significant improvement in transparency, 1998 and 2002. There is a strong reason to believe that IMF program had forced Indonesia's banking system to be more transparent. In fact, Wihardja (2009) shows empirically that countries that have been in crisis are relatively more transparent in holding other factors constant. Wihardja also shows that in the East Asian case, there is evidence that political rather than economic fundamentals influence transparency of central bank.

It is shown that more democratic countries, such as Japan and South Korea, tend to be more transparent than semi-democratic countries, such as Singapore, Malaysia, and Cambodia, which tend to be more transparent than non-democratic countries, such as China, Vietnam, and Myanmar. It is hard to disagree with the importance of political fundamentals on economic institutions. Precisely the establishment of an independent regional surveillance body is needed because reforming political fundamentals that are sovereignty issues is more difficult than reforming economic fundamentals. In other words, it will be too long to wait for countries to reform their political fundamentals. The question why we need a regional surveillance body in East Asia while we already have the IMF surveillance program is because IMF has its lost reputation in some of East Asian countries that they no longer want to borrow from the IMF.

There are certain issues that can best solved at the regional and global level. An example of this is regional infrastructures and climate change. What can Indonesia do to contribute to these regional and glob-

al institutions? Indonesia's contributions will rely on her own national institutions. In the economic sectors, behind-the-border economic and institutional reforms ranging from trade facilitation measure to reduce transaction costs (Soesastro 2008), microeconomic structural reforms to reduce poverty, inequality and unemployment, to legal and judicial reforms are priorities.

Since economic institutions are not independent from political institutions, improving the quality of our democracy from *de jure* to *de facto* is also important. At the more grass-root level, public facilitations, participations, and communications are also important. In order to set up an institution conducive to trade carbon rights, for example, public needs to be socialized and there has to be an agreement between the local government and the citizens as how to share the profit from carbon trading. Government also needs to communicate with the inhabitants in the case of protecting forests, which may require removals of these settlers.

INSTITUTIONS IN THE DEMOCRATIZED, DECENTRALIZED, AND GLOBALIZED INDONESIA

What is important to bear in mind is that reforming institutions is not about creating or changing rules but incentives. It is a system that consists of rules, stakeholders, beliefs, norms, and implied behaviour, which needs to be in equilibrium. It might be better to implement a second-best policy that achieves its goal than a first-best policy that never achieves its goal.

Global imbalance is not a cause but is an outcome of net savers and net spenders in the East and West reacting to different incentives to save and to spend. It is not the global imbalance that can be corrected but it is the incentives and the systems to save and to spend that can be corrected. In the economic sector, for example, before there is a self-insurance scheme to protect the economy from liquidity and reserve currency crisis, for example, East Asian countries will still be accumulating large foreign exchange reserves.

As long as a country, such as South Korea, accumulates large short-term debts, it will continue to accumulate large foreign exchange reserves. What might reduce South Korea's foreign exchange reserves are schemes that fund long-term growth, for example. In the case of

Indonesia, as long as people at large remain poor and uneducated, we cannot expect that they could participate in reforming political and economic institutions and hence, these institutions will remain highly influenced by the elites.

What we have also learned from the 1997 Asian Financial Crisis and the 2008 Global Financial Crisis is that liberalization without strong institutions is deadly. In the case of the 1997 Asian Financial Crisis, the crisis itself actually resulted from capital liberalization combined with weak banking institutions. Similarly, the 2008 Global Financial Crisis also resulted from financial liberalization combined with financial deregulation especially among the mortgage funds and hedge funds as well as credit rating agencies. This implies that democratization and decentralization in Indonesia without strong institutions, let it be political, economic and/or social institutions, can eventually have an adverse effect.

One aspect of institutions that we discussed above is information. To make institutions work, people need to have the correct beliefs, which points out to the importance of information. Asymmetry of information between citizens and leaders could make local institutions ineffective. Lack of transparency among countries in East Asia could render efforts towards regional financial integration not operational. Lack of transparency in the financial market creates uncertainties, which, because of people's aversion to uncertainty, may imply seemingly irrational behaviours.

Lastly, institutions are endogenous. That is the most difficult part. Transparency of economic institutions affects economic fundamentals, but the reverse is also true. Local governance affects district-level economic performance, but the reverse is also true. That is why we need exogenous factors to reform institutions. The question of what kinds of exogenous factors we need remain a challenge to economists and political scientists. Because of this endogeneity of institutions, reforming institutions must take into account social, political and economic frictions, to say a few. Similarly, reforming welfare must take into account institutional frictions.

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HOW HIGH IS THE GLASS CEILING?: MEASURING GENDER SENSITIVENESS OF SOUTHEAST ASIA'S TRADE LIBERALIZATION INITIATIVES[1]

Alexander C. Chandra

INTRODUCTION

As in many other parts of the world today, the impacts of the liberalization of the economies of Southeast Asia, particularly in the last decade or so, have become more pronounced. Overall, the impacts of trade liberalization in the region have been mixed, with some sections of the society come out as the winners, while others lose. For example, some would argue that the relative success of the economies of Southeast has been founded on a combination of sound, market-based and foreign investment-friendly policies (Rigg 1997, 3).

At the same time, however, economic liberalization also brings about multitude economic adjustment costs, normally at the expense of the poor and the marginalized section of the community. In its relation to the efforts to advance gender equality, however, it is fair to say that the policy-making process and implementation of trade policy has been generally far from being gender sensitive. In other words, it is not common that trade policy deliberation is pursued based on gender consideration. The prevalent argument among policy-makers

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[1] The electronic version of this paper will also available from the official website of the Trade Knowledge Network (TKN) at: http://www.tradeknowledgenetwork.net

is that trade policies and agreements generally affect people regardless of their class, race and gender. In nearly most of Southeast Asian countries, governments, in fact, only consult a narrow industrial interest in their trade policy deliberations.

All these are, of course, hardly surprising. Among other things, assessments on international trade and gender are relatively new (Senapaty 2003). Governments, particularly those in developing and least-developed countries, are equally slow in responding the different impacts of trade liberalization on men and women. Gender is certainly becoming an important factor in the complex relationship between trade, growth and development. By using a legal perspective in her analysis of the relationship among the aforementioned factors above, Mengesha (2006, 3-4) argues not only that there is a direct conflict between trade rules and the human rights of women, trade norms often undermine the effectiveness of norms on women. In the context of trade, as she further argues, what is often invoked in empirical research is the impact of trade rules on the capacity of the state to implement its obligations in economic and social life of its citizens. Because of the disadvantaged social status accorded to most women, trade policies and agreements often diminish the capacity of the state to protect, promote, and fulfill the economic and social rights of women.

Although it is true that trade can serve as a catalyst to promote greater gender equality, the impacts of trade liberalization and economic globalization on women, in particular, have so far been mixed. While, for example, on the surface trade liberalization has appeared to have improved women's empowerment and livelihoods,[2] many cases also show that the overall benefits accrued by women from trade liberalization have been somewhat marginal, often less than those acquired by men (McGill, 2004). Yet, in many circumstances, trade liberalization has in fact exacerbated gender inequalities and undermined the economic and social status of women (Margawati 2007).

In Southeast Asia, the impacts of trade liberalization are certainly far from being gender-neutral; in that it affects both men and women differently. Although trade liberalization is aimed, inter alia, to enhance competitiveness, the poor women in both developing and least-deve-

[2] See, for example, Nordas (2003).

loped countries of Southeast Asia are less likely to be equipped with the appropriate skills, technology and other resources which would otherwise enabled them to reap the benefits from trade liberalization. In contrast, poor women in these countries are often vulnerable to changes in the prices of agricultural and manufacturing products. With the current liberalization of trade , it is also often the case that these poor women are subjected to negative implications from the changes that emerge in the basic services, particularly health, that accompany this phenomenon.

As the region enters the twenty-first century, Southeast Asia has turned itself into one of the most open economic regions in the world. Countries are increasingly convinced that trade liberalization is crucial to their economic growth, and have subsequently reoriented their policies and budgets to improve the flows of goods and services that are exported and imported across borders (ICRW 2009, 3). Apart from being members of the World Trade Organization (WTO), countries in Southeast Asia are also pursuing trade liberalization within the regional framework under the auspices of the Association of Southeast Asian Nations (ASEAN), such as the ASEAN Free Trade Area (AFTA), ASEAN Framework Agreement on Services (AFAS), ASEAN Investment Area (AIA), and so on, and the wider East Asian (e.g., the projected East Asian Economic Community (EAEC) and the Asia-Pacific (e.g., the Asia-Pacific Economic Cooperation (APEC)) levels. In recent years, these initiatives have also been expanded through what most economists refer to as bilateralism, either in the form of Free Trade Agreements (FTA) or Economic Partnership Agreements (EPA) with trading partners. Southeast Asian bilateral FTAs and EPAs are mostly pursued with major developed countries (e.g., United States (US) and Japan) and/or regional groupings (e.g., European Union (EU)) from outside the region. These forms of liberalization tend to be wider in scope and coverage when compared to the negotiations at the WTO.

Again this background, this paper analyzes the gender-sensitivity of several selected trade liberalization initiatives pursued by the countries of Southeast Asia. Given the increasing relevance of ASEAN as one of the most aggressive promoters of trade liberalization initiatives in the region, this study also looks at the way in which women have been affected by ASEAN-led trade liberalization.

From the outset, this paper primarily argues that trade policies and agreements pursued by both ASEAN and its member countries are far from being gender sensitive. This is not to suggest that the absence of trade liberalization in the region would be a model of gender equality, and that trade liberalization is inexorably moving the position of women downwards. The analysis in this paper, however, suggests that, given the prevalent view among trade policy-makers that trade is gender-neutral, the absent of substantive consideration on the implications of economic opening towards the well-being of women risks undermining the sustainable livelihood of this dynamic group of the society.

The trade policies of ASEAN and its member countries are considered gender-sensitive if they: (1) put women at the centre of trade policy analysis and deliberations; (2) do not implicate the quality of the lives of the women in the region; (3) allow women better access to natural resources and social safety nets used to address adjustment costs deriving from trade liberalization; (4) involve trade-related capacity building to enable women participate actively in trade policy deliberations; and (5) are pursued along with the implementation of complementary gender advancement commitments.

In order to elaborate further the aforementioned argument, the paper is divided into several sections. Section two argues that gender should be considered an important element in the contemporary analysis of international trade. Section three provides general picture of the overall political, economic and social positions of women in Southeast Asia. Furthermore, section four analyzes several different types of liberalization initiatives that have taken place in Southeast Asia and the way in which these initiatives have impacted women in the region, while section five further identifies different advocacy groups that work around the issue of trade-gender linkages in the region. Finally, the paper concludes with a general overview of the key findings and key recommendations that should be incorporated in current and future trade negotiations.

THE PROMOTION OF GENDER EQUALITY IN TRADE POLICY-MAKING AND IMPLEMENTATION

Different Theoretical Approaches to Gender and Trade Nexus

Over the years, several approaches have been used to address the emergence and expansion of gender inequality as a result of trade liberalization. To start with, the Women in Development (WID) approach, which emerged from the liberal feminist movement that began in Europe and North America as a rejection of patriarchy and became a popular approach in the 1970s and 1980s, has the underlying rationale that women are an untapped resource who can provide an economic contribution to development (Moser 1993).[3] With the assumption that economic strategies often generate negative impacts to women, the approach argues that this group within the society should be brought into the development process through access to employment and the marketplace.

The WID approach is primarily focused on the policies and programmes that aim to alleviate the negative impacts of trade on women or to support their entry to the labour market (Randriamaro n.d., 30). Unfortunately, the WID approach gives too much emphasis on the activities that are reserved exclusively for women, thus excluding them from mainstream development activities (IFAD n.d.). Worse still, in its relation to trade-related issues, the WID approach fails to address the wider reforms that should be pursued at both the policy-making and systemic levels. In the mid-1990s, criticisms of the WID approach led to the elaboration of the Gender and Development (GAD) approach.

Unlike its predecessor, the GAD approach seeks to understand the causes of gender inequality within the context of relations between women and men that bring about gender disparity (Ministry of Foreign Affairs of Japan n.d.). Following the realization that the WID programmes, such as income generation, failed to move women out of poverty, the focus of analysis within the GAD framework was expanded to include local, national and global systemic issues (Centre of Concern n.d, 1). In

[3] The term 'Women in Development' was first coined in the early 1970s by the Women's Committee of the Washington, D.C., Chapter of the Society for International Development, a network of female development professionals. The term was subsequently adopted by the United States Agency for International Development (USAID) in their so-called Women in Development (WID) approach.

its approach to trade, GAD "acknowledges the unequal power relations between women and men in terms of access to the resources needed to participate in the trading systems, as well as in terms of distribution of their potential benefits" (Randriamaro n.d., 30).

Closely associated with the GAD approach was 'gender mainstreaming', which is a process by which the roles and relations of unequal power amongst gender is incorporated into the design and implementation of all policy programmes. Alternatively, it is also seen as "organizational strategy to bring a gender perspective to all aspects of an institution's policy and activities, through building gender capacity and accountability" (Reeves and Baden 2000, 2). Gender mainstreaming in the GAD approach utilizes gender analysis, which is the tool for analyzing the specific nature of gender differences by asking basic questions such as who does what, where, when, how often, with what resources and returns, and who controls what (ADB 2003). Such questions enable an assessment of gender differentiations in activities, resource ownership, use and control (Moser 1993). In other words, appropriate policies and strategies can be designed to improve the position of women through the use of information obtained from a gender-sensitive analysis.

The relationship between gender and trade has also been analyzed from the *'human rights approach'*. This approach was made popular during the 1999 WTO Conference in Seattle where civil society groups argued the WTO was prioritizing market forces and corporate interests over those of the governments, people and communities. Advocacy groups also argued that women's rights are human rights and that women experience injustices solely because of their gender. Later, this movement created a new paradigm which goes beyond the traditional a 'winners' and 'losers' analysis of mainstream trade theory to incorporate the social content of trade policies (Randriamaro n.d., 31). Although the human rights approach provided a strategic entry point for many gender advocates to advance their concerns *vis-à-vis* governments, international bodies, donor agencies and the wider civil society groups and networks, this approach is not always sensitive to gender given the notion of 'universality' attached to the human rights concept.

More recently, gender-oriented economic advocacy groups have pushed for an alternative approach in understanding the gender dis-

parities that persist within society. Based on a conflict model of a society, this approach focuses on the redistribution of resources through structural change. It mainly argues that conflict is a natural outcome of the unequal distribution of resources amongst different amongst different race, class, and gender (Moser 1993, 87). More importantly, advocates of this approach stress the importance of the political-economy of trade liberalization in the analysis of the nexus between gender and trade policy. In other words, the political economic approach to gender analysis would give importance "to the crucial need to link trade policy, fiscal, monetary, industrial and social policies alongside analysis of global inequalities in order to ensure that the Multilateral Trading System (MTS) supports the achievement of gender equality and sustainable human development" (Randriamaro n.d, 32).

Why 'Gender' Matters in Southeast Asia's Trade Policy

Trade policy-makers and practitioners in Southeast Asia are generally puzzled when asked about the importance of gender in trade policy. As mentioned earlier, there is a preconception amongst these state and non-state actors that trade is gender-neutral. However, there is now abundant literature that suggests otherwise; that trade policies affect men and women differently, most of which due to gender inequalities that persist between both sexes in terms of access to and control of economic and social resources and decision-making. Data in Table 1., for instance, shows the significant discrepancies between the estimated incomes of women and men in Southeast Asia, which still in favour of the latter. To a large extent, therefore, gender relations in Southeast Asia, as in many other developing parts of the world, are characterized by unequal power (Margawati 2007). What feminist scholars refer to as *'gender norms'* generally assign specific entitlements and responsibilities to men and women.

Consequently, gender norms determine the distribution of resources, wealth, work, decision-making, political power, and the enjoyment of rights and entitlements within the family as well as in public life (UNDAW 1999). Moreover, the division of labour is also gendered in the sense that certain forms of work, such as physical labour, cash-crop farming and managerial roles, are seen as the normal occupation of men, while care work and house work (e.g., cleaning, etc.), for exam-

ple, are highly feminized activities that are associated with the responsibilities of women, both at home and as an extension of their domestic tasks (Chen *et al.* 2005).

Table 1. Estimated Earned Income of Male and Female in ASEAN Countries (in US$)

Countries	Female	Male
Brunei Darussalam	15,658	37,506
Cambodia	2,332	3,149
Indonesia	2,410	5,280
Lao PDR	1,385	2,692
Malaysia	5,751	15,861
Myanmar	n.a.	n.a.
Philippines	3,883	6,375
Singapore	20,044	39,150
Thailand	6,695	10,732
Vietnam	2,540	3,604
ASEAN average	**6, 069.8**	**12,434.9**

Source: UNDP (2007/2008)

Feminist economists, such as Seguino (2006) and Hoskyns (2006), maintain that gender should be an important macroeconomic variable, and that gender relations can affect economic development and growth. The state of gender relations today, which, as mentioned earlier, frequently results in divergent outcomes between different genders, is already observable in several economic arenas in the Southeast Asian region, such as: (1) job segregation within the paid labour market; (2) the division of labour between paid and unpaid labour; (3) the distribution of income and resources within the household; (4) access to the redistribution by the state (e.g. access to education and social safety net programmes); and (5) credit in the financial markets. In general, therefore, the effect of the gendered economic opportunities show that men and women occupy different class positions, with the latter more likely to be poor, malnourished, less educated, and more overworked relative to the men (Davis 1981; Beneria and Roldan 1987).

It has become increasingly important to examine the nexus between gender inequalities and trade policies, and to take a broader

than usual view of development, poverty and well-being (Margawati 2006, 220). Among other things, the politicization of trade policy, the connection being made between trade and development and the expansion of trade to services, all have contributed to greater impact of international trade issues on the lives of normal citizens, including those of women (Hoskyns 2006, 2).

Unfortunately, mainstream economics literature, as mentioned earlier, is often gender-blind when it comes to assessing the relationship between trade, inequality and poverty. Although economists generally acknowledge that gender bias exists at the microeconomic level, such as in the operation of labour markets or the allocation of resources within households, they tend to see little relevance of gender at a macroeconomic or global level of analysis. Moreover, *social reproduction*, which is the term that is associated with the roles that women traditionally play, has been undervalued and not counted in the classical economic analysis (Picchio 1992; Hoskyns 2006, 3). This is mainly due to the general assumption that macro-economics is all about aggregates and that both policy objectives (e.g. price stability, employment generation, growth and external balance), and traditional policy instruments of macroeconomics (e.g., fiscal and exchange rate policies) are gender-neutral.[4] Similar views are often held with regard to the analysis of international trade and finance. Gender is, therefore, often ignored in theoretical, empirical and practical terms, thereby perpetuating gender biases in most economies.

Development economists, though, have been investigating the complex relationship between gender inequalities and trade liberalization for several decades. Although the effect of international trade on the gender wage gap and other aspects of discrimination is still unclear, a study conducted by Korinek (2005) finds that trade creates job

[4] It is not usual for trade theorists to be concerned with the detailed social consequences of trade liberalization. The general view is that trade is an activity that is good for the overall performance of the economy, even if it involves changes in the composition of economic activity which advantage some and disadvantage others. Trade theorists tend to argue that the effects of trade policy should be managed by other flanking policies. An example of this is the Trade Policy Review Mechanism of the WTO which investigates how the WTO's rules have been implemented by governments and their effects on the multilateral trading system, instead of on what effect international trade policy has generated in terms of the well-being of the world population. For a more detailed analysis on the reluctance of trade theorists to factor gender considerations into their work see, inter alia, Hoskyns (2006).

for women from middle-income developing countries. The question, however, remains as to whether trade liberalization which leads to an increase in women's share of paid employment in the export sector also generates higher incomes and greater empowerment for women more generally? It has been suggested that women's role in production becomes progressively less central and less important during capitalist industrialization in the developing countries (Momsen 2004, 173).

As industrialization proceeds, the so-called theory of *female marginalization* also argues that women are pushed out from higher-paid sectors into the relatively lower-paid and job status (Scott, 1986). Yet, statistical and sectoral indicators show that, in many developing countries, the expansion of industrialization has indeed led to the growth of women's share in employment (Margawati 2007, 221). The prevailing argument today, therefore, is that industrialization does not necessarily marginalized women. On the contrary, from the 1970s onward, an increase in women's share of employment seems to go hand in hand with successful industrialization in many Third World economies (Pearson 1997, 224-225).[5]

There is no doubt that economic openness and the development that follows have generated some positive impacts for women's daily lives However, women's position in the society remains unchanged. In many cases, in fact, the economic, social and political positions of women have even deteriorated as a result of economic liberalization (Kabeer 1994; WHO 2000). Again, data in Table 1 show that, despite decades of economic liberalization, the gap between the estimated incomes of women and men remain large. Although trade liberalization allows women to be more integrated into the labour force, there persists a gender-bias system that perceive women as inferior to men, which systematically manifest further in the forms of job segregation and wage inequality between the two sexes (Sinaga 2008).

Indeed, the removal of tariffs and quotas as a result of trade liberalization policies pursued by countries and regional groupings around

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[5] Pearson (1997: 225) further argues that a major feature of the Third World industrialization has been the employment opportunities that have been offered to women, though there has been much dispute as to why women are considered as the new industrial labour forces, and what such employment offered to women in terms of wages, training, promotion, working conditions, etc.

the world has generally exposed the previously protected sectors to competition and opened up new areas for exchanges and commoditization. New trade policies do not only generate changes in the employment trend, but also the patterns of prices, incomes and consumption, all of which affect men and women differently. Overall, suffice it to say that women may be affected by trade liberalization differently than men as a result of: (1) their asymmetric rights and responsibilities; (2) the reproductive and motherhood roles of women; (3) gendered social norms; (4) labour market segregation; (5) consumption patterns; and, finally, (6) time-poverty. While these characteristics overlap, they could also reinforce each other. To a large extent, therefore, men and women are confronted with different opportunities and constraints with the liberalization of trade and investment regimes in a society.

THE POLITICAL, ECONOMIC AND SOCIAL POSITIONS OF WOMEN IN SOUTHEAST ASIA

An analysis of the current political, economic and social position of women in Southeast Asia guides us to understand how well Southeast Asian women have fared in relation to their male counterparts. Table 2 provides various gender-related social indicators in the ASEAN member countries which are commonly used to measure the level of gender equality in countries all over the world. The United Nations Development Programme (UNDP)'s Human Development Index (HDI), Gender-related Development Index (GDI) and the Gender Empowerment Measure (GEM) are useful tools to measure the level of overall level of gender equality in the ASEAN countries.

The HDI ranks countries around the world based on their overall achievements in attaining the longevity, knowledge and the level of standard of living among their citizens. Inequalities between men and women, however, are better captured in the GDI and GEM indicators. While the GDI applies the same three basic dimensions as those used in the HDI, GEM is used to measure the inequalities between the opportunities accorded to both men and women in a country. Political and economic participation and decision-making, as well as the power over economic resources are some of the key components that make up GEM.

In general, as shown in Table 2, the levels of both development and gender equality throughout Southeast Asia remain diverse. Bru-

nei Darussalam, Singapore and Malaysia are the only countries in the region with a high level of human development (as measured by the HDI), while the remaining members of ASEAN are categorized with medium level of human development. What is apparent is that the promotion of gender equality appears to have improved along with the advancement of economic development.

Although GDI level data for Singapore is absent, other relatively higher income countries, such as Brunei Darussalam and Malaysia, score relatively high in their GDI level, each with the value of 0.886 and 0.802 respectively. The least developed countries of Southeast Asia, such as Cambodia and Lao PDR, on the other hand, record relatively lower GDI value at 0.594 and 0.593 respectively. Singapore is, in fact, within the top twenty countries in terms of the GEM ranking and value: in other words Singapore is the most progressive country in ASEAN in terms of the participation of women in the country's political and economic life.

Table 2. Gender Equality-Related Social Indicators of ASEAN Member Countries

Countries	HDI*	GDI Ranking and Value*	GEM Ranking and Value*	IMR*	MMR*	% of Women in the Parliament	Literacy Rate		Life Expectancy	
							Female	Male	Female	Male
Brunei	30	31 / 0.886	N/A	9.5	28.2	**	95.1	95.2	77.4	74.4
Cambodia	131	113 / 0.594	83 / 0.577	80.0	450.0	8.0	61.1	80.2	63.0	59.0
Indonesia	107	93 / 0.721	N/A	35.5	307.0	14.5	86.2	93.5	70.3	66.3
Lao PDR	130	114 / 0.593	N/A	82.0	530.0	N/A	60.9	77.0	56.0	54.0
Malaysia	63	57 / 0.802	65 / 0.504	6.3	30.6	N/A	88.4	88.4	75.9	70.3
Myanmar	132	N/A	N/A	44.7	150.0	N/A	92.9	93.7	64.4	61.5
Philippines	90	76 / 0.768	45 / 0.590	30.0	108.0	N/A	92.5	91.4	72.5	67.2
Singapore	25	N/A	16 / 0.761	2.5	30.0	6.5	91.4	97.1	80.9	77.0
Thailand	78	70 / 0.779	73 / 0.472	20.5	44.0	N/A	91.4	94.9	75.0	67.9
Vietnam	105	90 / 0.732	52 / 0.561	21.0	85.0	26.0	88.4	94.7	72.0	67.0

Note:
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HDI – Human Development Index
GDI – Gender-related Development Index
GEM – Gender Empowerment Measure ranking
IMR – Infant Mortality Rate (per 1,000 live births)
MMR – Maternal Mortality Rate (per 100,000 live births)
**

Currently, Brunei Darussalam does not have a parliament.
Source: UNDP (2007/2008) and ASEAN Secretariat (2006).

Furthermore, with the exception of Thailand, the democracies of Southeast Asia, including the Philippines and Indonesia stand at relatively modest positions in their HDI, GDI and GEM rankings and values. This simply suggests that, at least within the Southeast Asian context, democracy has not fully ensured women's participation in political and economic life in these countries. In Indonesia, the largest democracy in the region, women only occupy 14.5% of the seats in the parliament.

While it is true that the levels of life expectancy and literacy rates among Southeast Asian women have improved in comparison to their male counterparts, their participation in the political, economic and social decision-making process is still restricted. Further exacerbating the problems faced by Southeast Asian women today is, *inter alia*, the persistent social discrimination, including the resurgent patriarchies, such as the rise of conservative religious or ideological movements that often discipline women's mobility and sexualities.[6]

TRADE LIBERALIZATION AND ITS IMPLICATIONS FOR SOUTHEAST ASIAN WOMEN

Trade Liberalization in Southeast Asia

Trade liberalization is certainly not new for Southeast Asia. Although the region has been relatively a *reluctant* free trader as a whole, several member countries have pursued unilateral trade liberalization when they deem it suitable for their own development. Some parts of the region, particularly Singapore under the British administration, adopted free trade principles in the early 19th century. Although some countries have occasionally pursued protectionist policies in pursuit of self-sufficiency, the tradition of open economy remains today.

The concepts of open economy and free trade became more pronounced in the mid-20th century, and some countries, such as Myanmar and Indonesia, started to flirt with multilateral negotiations to remove trade barriers through their participation in the newly established Ge-

[6] As articulated by Josefa Gigi Francisco, General Coordinator Development Alternatives with Women for a New Era (DAWN) and the Senior Program Coordinator for Gender, Development and Economic Globalization (GDEG), Women and Gender Institute, Miriam College, in her electronic mail exchanges with the author on 25 August 2009.

neral Agreement on Tariffs and Trade (GATT).[7] Over the years, other Southeast Asian countries followed suit, and, to date, only Lao PDR has yet to become a member of the World Trade Organization (WTO), the successor of the aforementioned GATT.

A decade following the establishment of the Association of Southeast Asian Nations (ASEAN) in 1967, the five original member countries of the grouping, including Indonesia, Malaysia, the Philippines, Singapore and Thailand, agreed to embark upon closer economic cooperation by pursuing an ASEAN Preferential Trade Agreement (APTA). In order to improve economic cooperation among the members of ASEAN, the grouping also launched the ASEAN Industrial Joint Venture (AIJV), ASEAN Industrial Complementation (AIC), and the ASEAN Industrial Projects (AIP) to complement APTA. As time went by, APTA was transformed into the ASEAN Free Trade Agreement (AFTA) in 1992, and shortly after a number of other complementary measures to support open economic regime, such as the ASEAN Investment Area (AIA) and the ASEAN Framework Agreement on Services (AFAS), were also launched.

It was, however, the 1997/1998 economic crisis that served as the catalyst to propel ASEAN into one of the most open regional groupings today. It was not only that the crisis forced countries, such as Indonesia and Thailand, to undertake unilateral trade liberalization as prescribed by international financial institutions, such as the International Monetary Fund (IMF) and the World Bank, ASEAN, as a grouping, also took its own initiative to accelerate economic integration among its members. In 2003, for example, through the so-called Bali Concord II, the members of ASEAN agreed to launch the ASEAN Community, which comprises the ASEAN Political-Security Community (APSC), the ASEAN Economic Community (AEC), and the ASEAN Socio-Cultural Community (ASCC).

The ASEAN Community and its three pillars of cooperation are expected to be realized by 2015.[8] According to its 'Blueprint', which

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[7] Myanmar formally acceded as a member of GATT in 1948, while Indonesia entered the forum in 1950; a year after its independence was recognized by the international community.

[8] Initially, 2020 was decided as the target date for the achievement of AEC. At the 38th ASEAN Economic Ministerial Meeting (AEM), which was held in Kuala Lumpur, Malaysia, however, ASEAN economic ministers agreed to accelerate the establishment of AEC by 2015.

was agreed and signed by ASEAN leaders on November 2007, the AEC, which is the end goal of economic integration in the region, shall be implemented "in accordance to the principles of an open, outward-looking, inclusive, and market driven economy" (ASEAN Secretariat 2008, 5). In order to achieve its single market objective, ASEAN also thrives to incorporate the principles of free flows of goods, services, investment, capital and skilled labour.

The commitment towards pursuing open economic regime was also apparent through ASEAN and its member countries pursuance of Bilateral Free Trade Agreements (BFTAs) and Bilateral Economic Partnership Agreements (BEPA) with key dialogue partners, such as China, Japan, South Korea, Australia and New Zealand. To date, discussions on BFTAs and BEPAs with other key trade partners, such as the United States and the European Union (EU), are ongoing. Apart from presenting one of the world's most important geo-strategic locations, Southeast Asia has some 550 million consumers. These two factors have made the region very attractive for major developed countries. Overall, suffice it to say that open economic regimes, with trade liberalization as one of its components, remains as a key element in the effort of the region to pursue its economic development objective.

Trade Liberalization and Women in Southeast Asia

Trade liberalization and the overall process of economic globalization have had profound impacts on the livelihoods and well-being of women in Southeast Asia (Westley and Mason 1998). Indeed, Southeast Asian women now live in an environment that is continuously changing, while their livelihoods depend on being able to understand and challenges arising from global competition (Tonguthai 2007, 42). Overall, it can be argued that, although trade liberalization affects both men and women in the developing and least developed countries (LDCs) of Southeast Asia, women appear to have to bear the most the adverse effect of such a trade policy. In relation to trade liberalization initiatives that have been pursued by both ASEAN and its member countries, there are at least three sectoral areas of the economies where such adverse impacts of trade liberalization are felt the most by women in this region, which include those in the manufacturing, agriculture and services sectors. The following sub-sections highlight different complexities that are faced by Southeast Asian women in these sectors.

Southeast Asian Women and Manufacturing Sector Liberalization

Like most developing countries, women comprise a considerable proportion of employment in the manufacturing sector of many Southeast Asian economies.[9] Among other things, international production networks play a significant role in the rise of women's employment in the region (Francisco and Durano 2008, 171). In a similar line of analysis, Jomo (2001, 13) also argues that "the decline in the manufacturing employment set in for the first-tier or first generation East Asian [Newly Industrialized Economies (NIEs) at the time], encouraging [firms in these countries] to relocate low-skill labour-intensive production to the rest of Southeast Asia and China".

Following this trend, East Asian economies were transformed into an important production hub where countries in the region can be placed in the hierarchy within the international production networks (Ghosh 1998; Durano 2004). It is these production networks that have contributed significantly to the rise of women's employment, particularly through their presence in export-processing zones and in female labour-intensive sectors, such as garments and electronics (Wood 1991; Horton 1996; Standing 1999).

Data on the share of female workers in the manufacturing sector in selected Southeast Asian countries gathered by Jomo (2001, 14) support this analysis. In Singapore, for example, the share of female workers in the manufacturing sector rose from 18.2% in 1957 to around 40.2% at the end of last millennium. Similarly, in Malaysia, the proportion of female workers also rose significantly from 38.2 in 1980 to 47.6% in 1990 before declining to 40.3% following the 1997/98 financial crisis. Thailand and Indonesia also share this trend: in Thailand the proportion of female workers rose from 37.6% in 1960 to 49.3% in 1999, while in Indonesia the proportion of female in the manufacturing sector rose from 37.5% in 1961 to 44.8% in 1997.

[9] This is in stark contrast with the trend in the middle-income countries where, since the late 1980s, demand for women's labor in the manufacturing sector has been declining (UN 1999: 9). While it is far from clear as to why de-feminization occurs in these countries, the UN study also notes that in some East Asian countries, such as Singapore, Taiwan and South Korea, the composition of workforce in some manufacturing sectors, such as electronic, has seen the domination of male over female, particularly as the production shifts into more sophisticated products (e.g. computers and communication products).

More recent indicators of women's participation rate in the overall employment sectors of the region is also provided by the 2006 ASEAN Baseline Report produced by the ASEAN Secretariat (refer to Table 3). According to this report, female workers' participation rates across the region ranged from 46.3% (Indonesia) to 74.8% (Cambodia). The average participation rate of women in the labour force was 50.8%.

While the relative increase of the share of women's employment in the workplace has been regarded as a positive impact of trade liberalization in Southeast Asia, women's position in the society remains debatable. Feminist scholars, for example, observe a significant trade-off between gains in the quantity of female workers generated in industries and the losses of welfare associated with their poor working conditions (Francisco and Durano 2008, 172) and the quality of life of women and their households (Margawati 2007). It is common, for example, for female workers in Cambodia to experience sexual harassment from their male superiors and to find their paychecks cut with little or no explanation (Khus 2006).

Moreover, despite a broadly open economic regime, Indonesian women, on average, still earn only 76% of the salaries of their male counterparts (World Bank 2006).[10] Overall, Indonesian women are still over-represented in unpaid and low-paid jobs, but are under-represented in the more lucrative formal wage sector. Worse still, increased stress, the use of children as unpaid family labour, and the isolation from other workers, which inhibits collective organized action by women, are common problems arising from the impacts of trade liberalization in the informal sector in Thailand (Floro and Antonopoulous 2005).

In fact, Barrientos *et al.* (2004) also observe that there is a declining trend of the share of employment of women in the export processing zones in the Asia-Pacific region. Though it is true that women's share of employment in the region has generally increased, there is also another growing trend today where women are facing fierce competition from their male counterparts for the same job, particularly as the latter are more willing to accept lower pay to compete with women. To a certain extent, trade liberalization has certainly put into question the sustainability of women's position in the working environment.

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[10] See also Table 1 for data on the relative comparison of earnings between women and men in other Southeast Asian countries.

Table 3. Participation of Women in Production

Country	Labour Force Participation Rate (%)	Employment Rate of Women (%)
Brunei Darussalam	59.30	93.80
Cambodia	74.80	99.00
Indonesia	46.30	87.00
Lao PDR	74.50	98.30
Malaysia	47.70	96.40
Myanmar	48.60	95.00
The Philippines	51.00	89.70
Singapore	53.90	94.70
Thailand	63.90	96.60
Vietnam	48.60	95.50
ASEAN	50.81	91.15

Source: ASEAN Secretariat (2006: 72).

Southeast Asian Women and Agricultural Sector Liberalization

As with the liberalization in the manufacturing sector, similar liberalization efforts in the agricultural sector also bring about significant pressure for women. Agriculture is an important component of the economy of many developing countries, and Southeast Asia is no exception. In this region, the agricultural sector not only serves as a catalyst for export earnings and rural development, but it also underpins food security. Structural changes that come along with the introduction of trade liberalization often undermine the region's agricultural production in a sustainable manner. The expansion of industrialization as a result of the aforementioned structural changes from trade liberalization in Southeast Asia, for example, has propelled a significant shift in female employment from the agricultural sector to manufacturing and services industries. Not only that this shift has changed permanently the landscape of the rural economies in Southeast Asia (Rigg 1997, 219), it also requires governments in the region to reassess the ways in which food production can be sustained in the future.

Throughout Southeast Asia, the representation of women and men are also varied across different agricultural sectors, thus, impacts generated from policy changes, such as trade liberalization initiatives, to these sectors affect both sexes differently (García *et al.* 2006, 1). Apart from the fact that both women and men acquire different level of edu-

cation, skills and incomes, they are also placed differently in their role in the agricultural sector, and, as such, both sexes also posses different capacities to access and use agricultural resources. Indeed, a study conducted by Francisco and Durano (2008, 169) argue that, when trade volumes and values increase, control over agricultural traded commodities generally goes to men instead of women. Key to this analysis is the society's perception of what both authors refer to as *public* and *private* spheres and how both men and women are placed in these two spaces. In Southeast Asia, men generally dominate the public sphere, while women the private sphere. It is, they argue, common to find evidence of men to secure benefits from trade liberalization more than women.

In other instances, Rigg (1997, 244) postulates that the marginalization of women as a result of technological change generated from trade liberalization. For example, in Malaysia the use of combine harvesters and mechanical hullers in rice cultivation and processing has tended to displace women from their traditional role in agricultural production. It is not uncommon to find women looking for alternative employment beyond their village, or simply to retreat into housework (De Koninck 1992, 109-21). To a large extent, therefore, the technological changes are often accompanied by the decline of the importance of women in the agricultural sector (Parnwell and Arghiros 1996).

Southeast Asian Women and Service Sector Liberalization

Services sector liberalization plays a significant role in the integration of member countries in ASEAN as well as the integration of the region to the global economy. The services sector accounts for about 40 to 50% of the total GDP of many ASEAN countries (ASEAN Secretariat, n.d.). Apart from the WTO's services liberalization commitment, member countries in the region have also been cooperating to expand trade in this sector through the ASEAN Framework Agreement on Services (AFAS), as well as extensive plans for services' liberalization under the Bilateral Free Trade Agreements (BFTAs). Although AFAS follows the structure and approach of the General Agreement on Trade in Services (GATS) in the WTO, ASEAN aims that its liberalization in the services sector to go beyond what have been achieved at the multilateral level (or GATS-Plus).

The same also applies to most BFTA arrangements that both ASEAN and its member countries involve in. In this context, therefore, both ASEAN and its member countries are encouraged to pursue trade liberalization in services beyond what have been achieved at the GATS level. Within the AFAS framework alone, there are already seven services sectors, including air transport services, business services, constructions, financial services, maritime services, tourism and logistics that are targeted for full liberalization by 2015. Some ASEAN member countries also pursue unilateral liberalization in selected sectors of services as part of their commitments to pursue extensive liberalization with international financial institutions, such as the World Bank and the IMF. The case of health sector liberalization in Indonesia and Thailand is the case.

The overall approach towards the services sector liberalization within the frameworks of GATS, AFAS and the various BFTAs pursued by ASEAN and its member countries are likely to bring about disproportionately negative impacts to women, particularly poor women, in the region. Overall, there are at least two areas of concern in the area of services liberalization for the region's women: the liberalization of public services (e.g., healthcare) and what is normally referred to as the Mode 4 of services liberalization under GATS, or the movement of natural persons. In the area of health-related issue, for example, an analysis provided by the ICRW (2009, 2) suggests that, while trade liberalization in the services sector affects women positively as a result of new employment creation and the better access that is accorded to women to health services and technology, it may also lead to higher costs of health services and supplies, lower quality of services, and shortages of medical personnel due to the increase migration. The so-called *brain-drain* of medical professional to foreign countries could also further restrict poor women's, particularly those living in remote areas, access to proper health care.

The liberalization of tourism and entertainment industries provides another example where women's well-being and dignity can be jeopardized. Although tourism can be good development, particularly when it engenders a strong inflow of foreign exchange and positive inter-sectoral linkages that promotes growth of other sectors (Williams 2002, 4), it is very common to see the segregation of both

male and female in this sector as a result of gender stereotyping and sex segregations into different occupations.[11] In general, women also tend to predominate as the majority workforce in the relatively menial, semi-skilled, domestic and service-type occupations in this industry. Some observers, such as Francesco and Durano (2008, 174-175), would even argue that the commitment of most Southeast Asian countries to various services sector liberalization also raises the concern on the backward and forward sectoral linkages between tourism and entertainment industries and their links with prostitution and human trafficking. Indeed, as Williams (2002, 7) postulates, sex tourism has been raised as a key issue in the appeal of ASEAN destinations, and this particularly the case of Thailand and Cambodia where there are an influx of young girls from Indonesia, Myanmar and Lao PDR to work in bars and brothels.

Another aspect of services liberalization that risks undermining women's rights and well-being is the issue of migration. ASEAN includes both migrant workers' countries of origin and countries destination. Migrant workers from this region seek employment not only in the relatively more developed Middle-Eastern (e.g., United Emirates Arab, Lebanon) and Northeastern Asian countries (e.g.,Taiwan, Hong Kong, South Korea and Japan), but also in their ASEAN more developed neighbouring countries, such as Singapore and Malaysia. For migrant workers from countries in the Greater Mekong Sub-region (GMS), such as Cambodia, Lao PDR, Myanmar and Vietnam, Thailand is often the target country of their destination.

Among the growing trends in the current migration pattern of Southeast Asia is feminization, which mainly due to the rise of number of women seeking work outside their home countries.[12] In the Philippines and Indonesia, for example, the comparative distribution

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[11] Williams (2002: 4) also adds that the conventional wisdom that tourism is unambiguously good is problematic for several reasons. Firstly, it does not recognize the drain of resources and loss of revenues in the tourists-sending countries. Secondly, it often ignores distributional and other key factors associated with the goods and services used by the tourists. Finally, it also ignores the social, gender equity and environmental impacts of tourism.

[12] The issue of the feminization of women began to emerge in the 1980s among women's rights advocates who called on governments and migrant rights policies to pay more attention on the gender aspects of migration, particularly around the failure of the programs and policies to address specific vulnerabilities of women migrant workers (Carling 2005).

of male and female migrant workers over time is quite striking (Gois 2008, 123-124). In the Philippines alone, the percentage of distribution of female and male migrant workers in the early 1990s were nearly the same, both account for about 50% of the total migrant workers sent by the country. By 2002, the number of Filipino women leaving their home country to seek employment abroad rose to 70%, while the percentage of their male counterparts declined to about 30%. In Indonesia, by contrast, although the percentage distribution between female and male workers remains relatively the same over the period of 1992 to 2002, the distribution gap between the two sexes is very wide, or roughly 65% for female and 35% for male workers. In Cambodia the percentage distribution of female and male migrant workers stayed at an average of 50% each in the early 1990s, but the percentage distribution for female migrant workers increased to 51% in 2002, while the percentage distribution of their male counterparts declined to 49% in the same year.

Overall, there are a number of factors that lead to the increase feminization of migration today (Gois 2008, 122-123). First, as a result of massive demand for cheap labour from poor and developing countries, there has been an increase number of women who independently seek employment abroad (INSTRAW 2007, 2). Second, the demand for more women workers in some sectors enables women to augment family incomes, which provides added incentives for women to migrate for work. Third, there is also the emerging *'mail-order bride'* phenomenon, which normally involves women who publish their intent to marry someone from another, usually more financially-developed, countries. This phenomenon is certainly common in many Southeast Asian countries, particularly in the Philippines and Vietnam. In 2004, for example, the statistics produced by the Taiwanese government suggests that Vietnamese women account for 69.8% of female foreign spouses.[13]

Despite their increased importance to the economic development of the region, female migrant workers remain marginalized in the regional economic integration initiatives within and beyond ASEAN. A major absence in the social dimension of ASEAN, as Chavez (2007,

[13]As quoted in Gois (2008, 123).

369) argues, is the non-recognition of low and unskilled labour in official discussions and as a target for regional action. A number of frameworks for Mutual Recognition Arrangement (MRA) carried out to complement the AFAS agreement, such as the ASEAN MRA Framework for Accountancy Services, the ASEAN MRA on Architectural Services, and so on, for example, are targeted to cater the economic interests of skilled and professional migrant workers. A number of migrant workers advocacy groups have raised this point to ASEAN policy-makers. For example, Philippines migrant workers advocates argue that Mode 4 of GATS approach adopted by ASEAN in its AFAS agreement is not inclusive (Rivera 2005). Instead of recognizing the importance of semi-skilled and unskilled labour, ASEAN's adoption of GATS approach reflects only an existing structural and institutional bias against the majority of migrant workers from this region.

Another gender-related aspect that is still out of ASEAN's primary consideration is undocumented or irregular migration (Gois 2008, 125-126). Though it is difficult to obtain reliable statistics documenting the number of undocumented migrant workers in the region, the estimated numbers of women involve in irregular migration remains significant. In 2000 alone for example, it was estimated that there were 1.8 Filipino migrant workers abroad, with many of these irregular migrants were women (AMC and MFA 2000). So far, the recognition of undocumented migrant workers is limited to the recognition of trafficking in persons. The invisibility of undocumented migrants from the official policy of ASEAN does not only preclude these groups from the potential advancement of economic integration, but also endangers health initiatives of ASEAN, especially in regards to the prevention and control of communicable diseases, such as HIV/AIDS and avian flu (Chavez 2007, 370). Indeed, as pointed out in studies conducted by Cheng (2005) and the International Organization for Migration (IOM) (2005), undocumented migrants are disproportionately more exposed to health risks due to inadequate working conditions and irregular movement.[14] The same studies also suggest that undocumented migrants are less likely to seek medical attention when they are ill because of their status.

[14] As quoted in Chavez (2007, 370).

WOMEN, GENDER-ORIENTED PRESSURE GROUPS AND TRADE POLICY-MAKING IN SOUTHEAST ASIA

Southeast Asian Women in Trade Policy-Making

Advocates of neo-liberal economic policy generally claim that trade liberalization is an important prerequisite for national reform.[15] In the context of Southeast Asian women, however, trade liberalization has not necessarily been accompanied with the necessary reforms to advance their position in the society. As mentioned earlier, the preconception among Southeast Asian trade policy-makers that international trade is gender-neutral contributes to the exclusion of gender considerations in the region's trade policy formulation. Although there are scant analyses given to the role of women in ASEAN-specific trade policy-making process, a number of studies focusing on trade policy deliberations in ASEAN and each of its member countries provide a glimpse at the way in which trade policy-making takes place in the region.[16] Although, as shown throughout this paper, the analyses on the impacts of trade liberalization on women, or gender disparity in particular, are vast; none of the trade policy-making studies on Southeast Asian region consider gender aspects, the role, concerns and aspirations of women as integral parts of trade policy deliberations in the region.

There are several reasons to explain the scarcity of gender considerations in Southeast Asia's trade policy-making literature. First, there is an increasing agreement amongst critical scholars and observers of international trade in the region that trade policy still remains within the realm of economic-elites (Chandra and Chavez 2008a; 2008b). Second, international trade is still perceived as predominantly an issue of concern to economic actors. In the relatively more democratic political regimes of Southeast Asia, such as Indonesia and the Philippines, business groups and associations and large conglomerates have tradition-

[15] See, for example, Soesastro and Basri (2005) and Shafaeddin (2005).

[16] In 2005, for example, *the ASEAN Economic Bulletin* 22, no.1 issued a special edition that gave extensive analyses on the way in which trade policy-making processes are being made both at regional- and country-level in Southeast Asia. A study conducted by Chandra and Chavez (2008) also looks at the role of civil society in ASEAN's integration as a whole. Meanwhile, for more country-specific critical analysis see, *inter alia*, Chandra (2005; 2007; Forthcoming).

ally been considered as key stakeholders in trade policy deliberations. In most Southeast Asian countries, the academic community also plays instrumental role in assisting the design and formulation of their governments' trade policies. Third, the two above-mentioned reasons contribute to the generally weak dissemination of relevant information on trade policy issues in many Southeast Asian countries. Fourth, when information is available, women, particularly poor ones, are often unable to engage in full debates on the technical issues related to the trade policy of their countries.[17] Finally, although there are now increasingly economic-literate women in the society, there are always, as mentioned in some parts of this paper, social barriers that prevent them to making meaningful contributions to the formulation of trade policy.

Having said this, it is interesting to note that some of the high profile economic-related policy-makers in the region are women. In Indonesia alone, for example, high profile women, such as Dr. Sri Mulyani Indrawati and Dr. Mari Elka Pangestu, hold control of strategic economic ministries within the country, with the former is currently heading the Indonesian Ministry of Finance, while the latter is currently serving as the Minister of Trade for the country. In Malaysia, Rafidah Aziz was the country's Minister of Trade and Industry for twenty years, from 1987 until 2008, while Eleanor Briones served as the Treasurer for the administration of Joseph Estrada in the Philippines (1998-2001). Even more so, some women even held top positions in the political structures of some ASEAN member countries. Two women, for example, including Corazon Aquino (1986-1992) and Maria Gloria Macapagal-Arroyo (1998-present), have taken the leadership of the Philippines. Equally, in Indonesia, Megawati Sukarnoputri, the daughter of the country's first President, Sukarno, also held the top leadership from 2001 until 2004.

Although it is not uncommon for women to hold very high positions in the political and economic life of countries in Southeast Asia, there is little evidence that these women leaders advance the interests of women as far as trade policy is concerned. Indeed, it was under

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[17] As articulated by Hira Jhamtani, Associate for Asia and Indonesia of the Third World Network (TWN), in her electronic mail exchanges with the authors on 26 August 2009.

the administration of President Arroyo that the Philippines embarked upon aggressive trade and investment liberalization under the frameworks of regional and bilateral free trade and economic partnership agreements. In Indonesia, the administration of President Megawati also pushed for the country's entrance into the ASEAN-China Free Trade Agreement (ACFTA) without formal ratification from the parliament (Pambudi and Chandra 2006).

Moreover, the current Finance and Trade Ministers of Indonesia, Dr. Sri Mulyani and Dr. Pangestu respectively, are also known as neoliberal advocates who have been promoting further liberalization in the country to expand national reforms that have been achieved by Indonesia. While debate is still on-going as to whether trade liberalization is harmful to the livelihood and well-being of women, it is clear that women's participation in top policy-making process does not necessarily advance women's economic interests. Or, if there are, indeed, signs of improvement in the well-being of women, they do not necessarily result from gender-specific considerations in the formulation of trade policy.

Gender-Oriented Pressure Groups in Southeast Asia's Trade Policy-Making

While women's participation in top trade policy-making level fails to advance the economic interests of women, there are some advocacy groups that actively push for trade policy reform, both at the national and regional levels. However, the number of these advocacy groups remains minimal at both levels. One of the most active gender-specific trade advocacy groups or networks in the region is the International Gender Trade Network (IGTN). It is a network of gender specialists, hosted by the Philippines-based Gender, Development and Economic Globalization (GDEG) of Miriam College, that provides technical information concerning gender and trade issues to women's groups, NGOs, social movements and governments.[18] Scholars and activists from both IGTN and GDEG pursue active advocacy works around national and regional trade and gender issues in Southeast Asia. Another relatively

[18] Further information concerning the IGTN is available from its official website at (accessed on 30 August 2009): http://web.igtn.org/home/

active gender advocacy network is the Thailand-based Asia-Pacific on Women, Law and Development (APWLD), which attempts to promote gender equality from a human rights perspective. Its programmes on 'women and environment' and 'labour and migration' are often interlinked with trade liberalization initiatives at the multilateral, regional and bilateral levels.[19]

Aside from the aforementioned gender-specific advocacy groups, there are also a host of different regional advocacy groups that do not necessarily work on gender and trade linkages specifically, but have either a programme or research or advocacy projects around this issue. NGOs and alternative research networks, such as the Third World Network (TWN), Migrant Forum in Asia (MFA), The Coordination of Action Research on Aids and Mobility (CARAM) Asia, Focus on the Global South and the Asia-Pacific Research Network (APRN), are the examples of such advocacy groups or networks. Although, for instance, the TWN's primary focus is in the area of trade and development-related issues, the Network has specific research agenda linking gender and economic issues.[20]

Meanwhile, the MFA has also been active with their partner organizations at both national and regional levels in promoting the rights of women migrant workers under the various trade liberalization initiatives pursued by ASEAN and its member countries. Similarly, CARAM Asia is also a regional network that tackles migrations issue, but it has a more specific focus on health policy. In relation to trade liberalization, this particular network works to strengthen the analysis, perspectives and awareness around globalization, the WTO and the International Financial Institutions (IFIs).[21] Furthermore, scholars and activists from the Focus on the Global South have also carried out research projects that touch upon the linkages of trade liberalization and

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[19] For further details concerning the APWLD's work programs that touch upon the gender and trade linkages, visit its official website at (accessed on 30 August 2009): http://www.apwld.org/programs.htm

[20] For the range of gender and economic-related issues advanced by the TWN, see, for example, its official website at (accessed on 1 September 2009): http://www.twnside.org.sg/women.htm

[21] For further details concerning the program of CARAM Asia in the area of trade liberalization and migration, visit the official website of CARAM Asia at: http://www.caramasia.org/index.php?option=com_content&task=view&id=200&Itemid=328#MHG, accessed on 1 September 2009.

gender issues.[22] And, finally, the APRN has also carried out a research project on the issue of the impact of globalization on women labour.[23]

It is, however, more difficult to find gender-specific advocacy groups that pursue advocacy work on trade-related issues at the national level. Likewise, it is equally a painstaking task to identify general advocacy groups that have specific programmes or projects on gender-trade linkages. In Indonesia, for example, although gender-oriented advocacy groups have blossomed since the early 2000s, there are only a handful of these organizations that have some interest in engaging in debates on trade policy. One of such organizations is Women's Solidarity (SP–*Solidaritas Perempuan*), which has a specific programme on women and food sovereignty.[24] While the type of stakeholders involve in trade policy deliberations vary across ASEAN countries, there are probably only four countries that have active national trade advocacy pressure groups, and these are Indonesia, Malaysia, the Philippines and Thailand.

Given the extensive coverage of trade liberalization issue these days, gender equality and international trade linkages are often overlooked as key programmes of these national-level trade advocacy groups. Trade-specific advocacy groups in these countries, such as the Institute for Global Justice (IGJ) of Indonesia, the Monitoring Sustainability of Globalization (MSG) of Malaysia and the FTA Watch network of Thailand, all generally have small or weak programmes dedicated on trade and gender linkages.

Although the issue of gender equality is gaining more importance in the region, advocacy work around the gender equality and international trade linkages is stronger at the regional than the national level. As mentioned earlier, the issue of gender equality in general is still a matter of key concern for many national gender-oriented groups in Southeast Asian countries. Moreover, despite extensive analysis on the linkages between gender equality and international trade, the issue is

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[22] See, *inter alia*, Chavez (2007).

[23] For further details of this project, visit the official website of the APRN at: http://www.mfasia.org/mfaActivities/MFASchedActivities2007.html, accessed on 1 September 2009.

[24] For further details of this program, visit the official website of the SP at: http://www.solidaritasperempuan.org/index.php?option=com_content&view=article&id=54&Itemid=60&lang=en, accessed on 1 September 2009.

not always obvious for many national-level gender-oriented organizations. In other words, the priority given to the international trade issue among national-level gender-oriented advocacy groups is still relatively low.

The same can also be said about national-level trade-specific advocacy groups where their commitment to work on gender equality and international trade linkages remain modest. Given this reality, therefore, there is little doubt that gender equality is still far from being a major factor in trade policy consideration at both national and regional levels in ASEAN. While challenging, there is certainly an ample space in which the issue of gender equality could fit into the trade policy processes in the region.

Table 4. Gender-Trade Advocacy Groups in ASEAN

Gender-Specific Organizations with Trade Programmes / Projects		
Organization	Geographical Scope	Focal Issues / Activities
International Gender Trade Network (IGTN)	International, regional and domestic	The Network primarily pursues research and advocacy on the linkages between gender and regional and global economic integration.
Development Alternatives with Women for a New Era (DAWN)	International and regional	The organization mainly works on gender-related issues, and it has provided a research input to the ASEAN-related institutions on gender and trade.*
Asia-Pacific Women, Law and Development (APWLD)	Regional	The organization covers wide area of activities, including: rural and indigenous women; women and environment; violence against women; Women's participation in political process; labour and migration; and Cross-cutting initiatives.
Women's Solidarity (SP – *Solidaritas Perempuan*)	National (Indonesia)	The organization works primarily on the promotion of gender equity, but it also has specific programmes dedicated on gender and natural resources and gender and food sovereignty.
Non-Gender-Specific Advocacy Groups with Gender-Trade Linkages Programmes / Projects		
Organization	Geographical Scope	Focal Issues / Activities
Third World Network (TWN)	International, regional and domestic	Primarily working on trade and sustainable development-related issues, but also has a specific programme on *women and gender*, which covers issues such as: (1) gender and global economic issues; (2) gender and health; (3) gender, media and culture; and (4) gender, land and resource use.
Migrant Forum in Asia (MFA)	Regional	The Forum primarily works on addressing migrant-related issues, but it also has an initiative to create alternative sustainable economic models, processes and practices for migrants.

Coordination of Action Research on Aids and Mobility (CARAM) Asia	Regional	As a network organization, CARAM Asia generally coordinate research and advocacy works on migrants' state of health, foreign domestic workers, and so on. The network also works on migration, health and globalization issues.
Asia-Pacific Research Network (APRN)	Regional	The Network pursues coordinated research among members on economic liberalization-related issues. It has also initiated a coordinated research project on the issue of globalization and women labour.
Focus on the Global South	International	Focus generally works on trade liberalization and globalization-related issues, but it also assigns some individual staffs to work on trade and gender-related issues.
Institute for Global Justice (IGJ)	National (Indonesia)	The organization pursues research and advocacy on economic globalization issues.
Monitoring Sustainable Globalization (MSN)	National (Malaysia)	The organization pursues research and advocacy on the issues of economic globalization.
FTA Watch	National network (Thailand)	The Network is primarily used to advocate issues concerning trade liberalization in Thailand. Apart from the country's critical intellectuals, the Network also involves the participation of women-related organizations interested to pursue collective actions against FTA initiatives involving Thailand.

Note:

* DAWN pursued one region-wide study in 2006 for the ASEAN Secretariat.

Source: Various official websites of the mentioned organizations and networks (accessed on 3 September 2009).

CONCLUSION

There is little doubt that trade liberalization has generated profound effects to the well-being of women in Southeast Asia. Not all of these impacts are negative, however. Indeed, the opening up of the region's economies, at both national and regional levels, has brought about new opportunities in the form of new employment, which may allow them to access higher income level and improve their status in the society. In line with the region's commitment to achieve the Millennium Development Goals (MDG) in which gender equality is one of its core components, efforts to improve gender equality have also improved recently.

Given their increasing role in the economies of Southeast Asia, however, women are often found as the major victims of economic openness. Poor women, in particular, remain vulnerable to economic policy changes that occur in the region. Unfortunately, trade policies

are often gender-blind and ignore women's interests and aspirations. As a result, it is not uncommon to find that trade policies adopted and pursued by both ASEAN and its member countries further marginalize women in the society.

Given such circumstances, there are a number of policy recommendations that could improve the position of women in trade and trade policy-making. First, women, along with other marginalized economic actors, should be put at the centre of trade policy analysis and deliberations in the region. As mentioned earlier, women increasingly play significant roles in the economies of Southeast Asia. Any trade policy changes that affect the society at large must take into account the concerns and aspirations of women's groups. Second, trade policy changes should not be made at the expense of the quality of the lives of women in the region. Southeast Asian women do not only contribute to the economic development of the region, but also to the maintenance of healthy family life that contributes to social and, potentially, further economic stability of the society.

Third, as a regional organization, ASEAN could improve its gender-sensitiveness by ensuring commitment to undertake the necessary gender-oriented review of its trade liberalization initiatives as currently done by other regional groupings, such as the Southern African Development Cooperation (SADC).[25] Fourth, women should be given easy access to any social safety nets schemes initiated by ASEAN and its member governments, should the adjustment costs generated from trade liberalization prove greater than its benefits.

Fifth, trade-related capacity building is a very crucial element in the efforts to promote gender equality in the region. Although women are often both the beneficiaries and victims of trade liberalization, they often lack the capacity to either reap the benefits or minimize the negative impacts from such a trade policy. Empowering women in trade policy formulation is a necessity for sustainable economic development in the region. Moreover, capacity building to eradicate discrimination against women in the society is equally imperative. In many

[25] Article 17(7) & (2) of the SADC's Gender and Development Protocol specifies that member states have the deadline of 2015 to: (a) review their trade policies, protocols and declarations to make them gender responsive; (b) include regional women's networks in trade policy structures; (c) create gender quotas in all

Southeast Asian communities, women are still perceived as second-class citizens. In the absence of such efforts targeted at the community at large, women would still likely be the subject of harsh and persistent discrimination, which might either hinder them from gaining from the positive impacts of trade liberalization or expose them from its negative impacts.

Finally, the implementation of various commitments adopted by ASEAN and its member countries to improve gender equality, such as the 1988 'Declaration on the Advancement of Women in ASEAN' and others, is critical to the well-being and welfare of the region's women. However, commitment alone is certainly not sufficient without the appropriate amount of resources to support their implementation.

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RECENT INDONESIA'S ECONOMIC GROWTH AND TRADE PERFORMANCE

Fajar B. Hirawan and Widdi Mugijayani

GENERAL OVERVIEW

Indonesia's economy showed uncertainties in the mid of 2008. These uncertainties persisted in the first semester of 2009 as the global financial crisis still continues to threaten the national economy aggravated by the slump in other economies around the world. After the East Asian Financial Crisis 1997–1998, Indonesia recovered with a stable and resilient economy against both internal and external shocks. The government's objective is not only about economic stability, but also about achieving high rates of growth. The economy slightly continued to escalate and had been on the right track to meet the achievement of the high rates of growth until Q2-2008. Following this, the GDP growth reached the highest level by 6.4%. But, the economy started to undergo turbulence in the second semester of 2008, in particular in October 2008, as stock markets worldwide crashed and entered a period of high volatility. Consequently, the economic activities were slowing down because of the global food-crude oil force and the financial crises in the region.

In line with the substantial amount of capital outflow from Indonesia, the exchange rate of Rupiah (IDR) against the US dollar (USD) suffered depreciation with high volatility in the end of 2008 and then gave a positive signal, appreciation since April 2009 or after legislative

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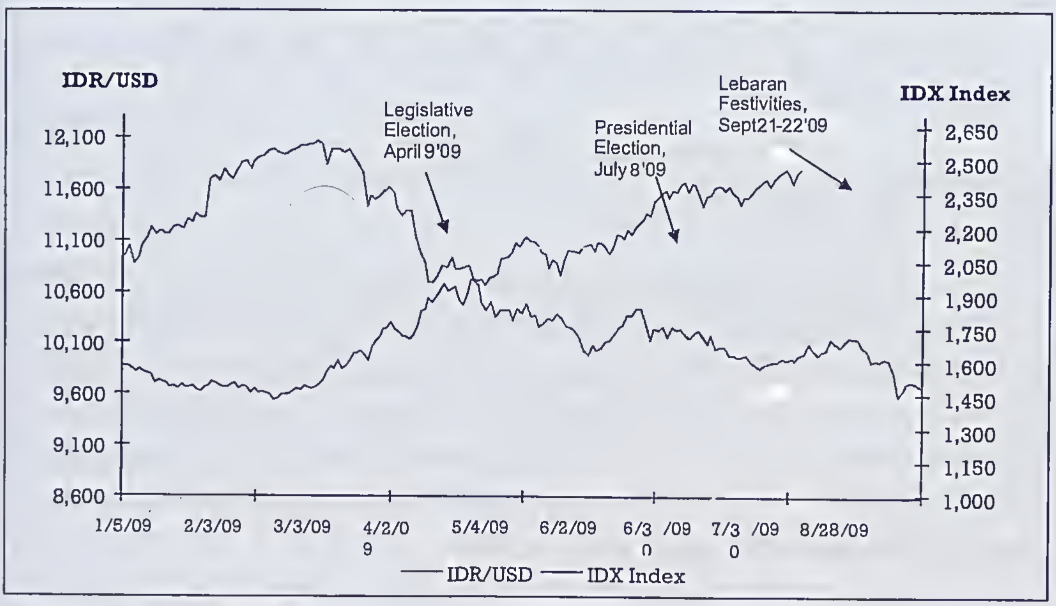
election. This condition might become an alarming indicator for Indonesia's trade performance and give a pressure for the inflation. The appreciation of Rupiah became negative, especially in terms of supporting export. During the year 2008, the domestic financial market performance, Indonesia Stock Exchange (IDX), fell quite significant up to 50% in the end of 2008. But, it started to experience the bullish trend since Q1-2009 (see Figure 1). After the legislative and presidential elections, Indonesia's composite index rose sharply and reached the highest level at 2,400 in Q3-2009, especially in September 2009. It was contributed mainly by the growing positive sentiment of global financial market recovery in which the movement of stock market was in line with the trend of regional stock markets given the relatively high foreign exposure of the country's financial market.

Figure 1. Exchange Rate and IDX Index, January-September 2009

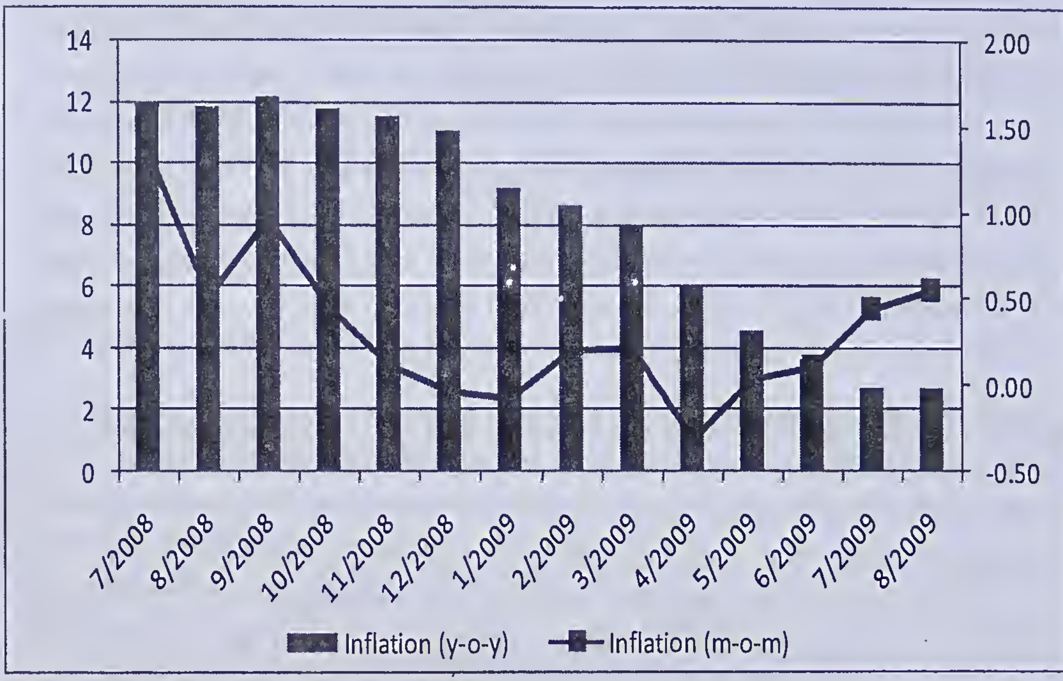


Source: CEIC Asia database

Nevertheless, the inflation was mainly stable because of several factors, such as the decrease of fuel and commodity prices, the stable stock of staple foods, especially rice, and the significant decline of imported inflation, that did not affect Indonesia's economy. The inflation shocked only when the special occasion took place in Indonesia, like Eid Mubarak celebration. During July 2008 until August 2009, the in-

flation rate (y-o-y) tends to decrease from 12% in July 2008 to around 2-4% in the mid of 2009 (see Figure 2).

Figure 2. Inflation Rate, July 2008 – August 2009 (in Percent)



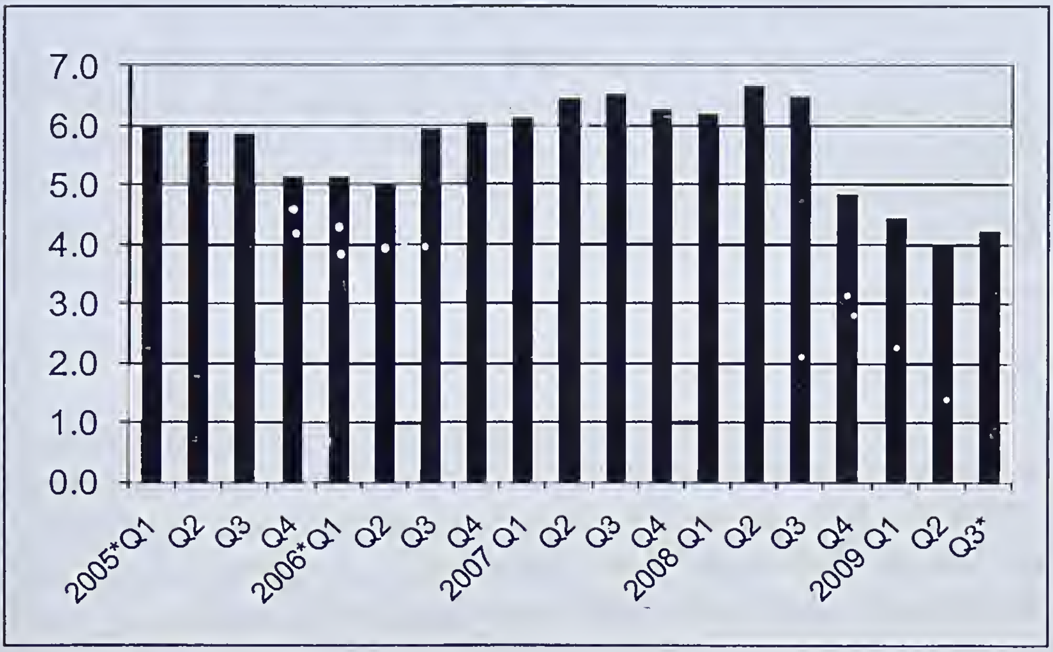
Source: International Monetary Fund (IMF)

However, based on the balance of payment (BOP), in 2008, the most sensitive indicator that suffered from the global financial crisis was international trade. Even though Indonesia deserves a surplus trade based on exports growth (y-o-y), it tends to decline since September 2008. Fortunately, the Indonesia's trade performance began to show the positive trend since April 2009 as the momentum of crisis recovery took place throughout countries.

ECONOMIC GROWTH

Beginning from Q4-2008, as the global financial crisis taking place, until Q1-2009 the rate of Indonesia's GDP growth has been steadily decreasing. It reached the lowest level by 4% in Q2-2009 (see Figure 3). Yet, the increasing trend in Indonesia's GDP growth started in Q3-2009. Based on that condition, the third quarter of 2009 was the momentum of the economic recovery in Indonesia after the global financial crisis turbulence that happened in Q4-2008.

Figure 3. Indonesia's GDP Growth, 2005 – Q3-2009 (y-o-y) (in Percent)



Source: Bank Indonesia

Expenditure Side

In 2009, Indonesia's economic growth on the expenditure side shows a drastic falling rate. From Q1-2009 until Q3-2009 (q-to-q) Indonesia's growth rate decreased as compared to the same period in 2008. Indonesia's GDP went down sharply from 5.2% in Q4-2008 to 4.4% in Q1-2009. It keeps falling to 4.0% in Q2-2009, but increased slightly in Q3-2009 to 4.2%. The decline in the growth rate was caused mostly by the decrease of overall consumer's ability to spend money, which in turn affected the trade sector components in GDP—export and import. However, the trend of recovery, especially in trade, has been on the go since Q2-2009 due to an increase in trade components.

The increasing proportion of government consumption is made artificially on purpose to stimulate the growth by giving fiscal stimuli to overcome the effects of financial crisis. Table 1 shows a very high gap between the percentage of government consumption in the first quarter of 2008 (3.6%) and the first quarter of 2009 (19.3%). Meanwhile, the household consumption remains constant, although it has been decreasing during Q2 and Q3 of 2009.

Table 1. GDP Growth Components: Expenditure Side (y-o-y) (in Percent)

Items	2008				2009		
	Q1	Q2	Q3	Q4	Q1	Q2	Q3*
Household Consumption	5.7	5.5	5.3	4.8	5.8	4.8	4.9
Government Consumption	3.6	5.3	14.1	16.4	19.3	17.0	11.4
Gross Fixed Capital Formation	13.7	12	12.2	9.1	3.5	2.7	3.2
Export of Goods and Services	13.6	12.4	10.6	1.8	-19.1	-15.7	-12.4
Import of Goods and Services	18	16.1	11	-3.5	-24.1	-23.9	-20.3
GDP	6.2	6.4	6.4	5.2	4.4	4.0	4.2

Source: Bank Indonesia

Production Side

The production side of Indonesia's GDP experienced a slower pace during Q1 and Q2 of 2009 (q-to-q) compared to the same period in 2008. The Indonesia's GDP began to increasingly grow in Q3-2009,, even though the impacts of the global financial crisis still affect several sectors, such as trade, hotel, and restaurant, manufacturing, and agriculture. Meanwhile, the rest of the sectors succeeded to show the stable growth progress, even the positive growth like electricity, gas, and water (see Table 2).

The transportation and communication sector showed the most decent and rather stable pattern during 2008–2009 and it also posted the highest growth at 16.5% in Q3- 2009 resulting from the annual change. However, in general, the GDP growth by production side was burgeoning in Q3-2009 and it showed stable and positive sign in the economy.

Table 2. GDP Growth Components: Production Side (y-o-y) (in Percent)

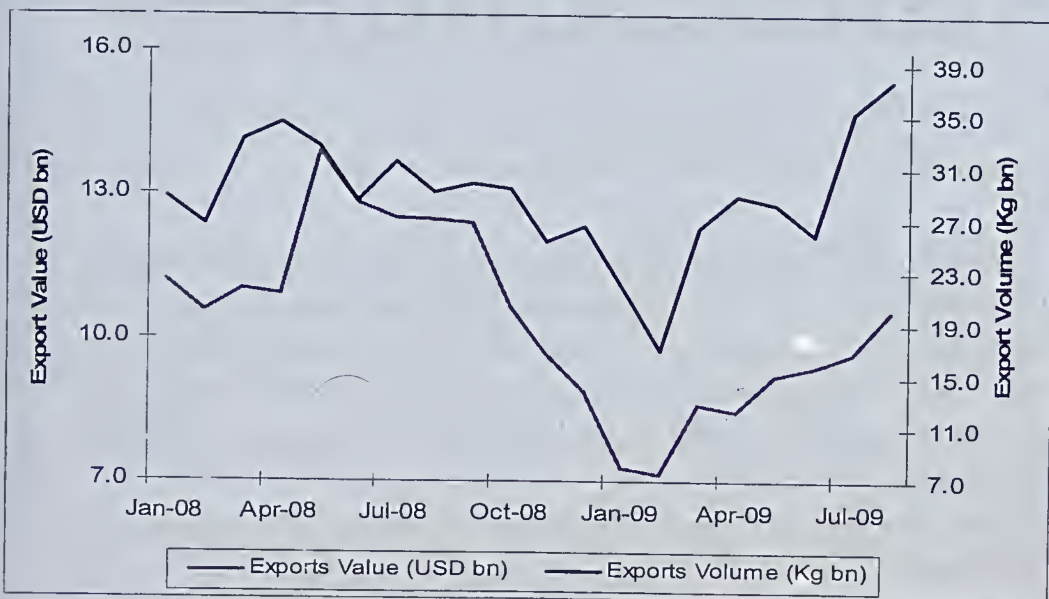
Items	2008				2009		
	Q1	Q2	Q3	Q4	Q1	Q2	Q3*
Agriculture	6.3	4.8	3.4	4.7	4.8	2.4	2.2
Mining and Quarrying	-1.7	-0.5	2.1	2.1	2.2	2.4	2.2
Manufacturing	-4.3	4.2	4.3	1.9	1.6	1.5	1.7
Electricity, Gas, and Water	12.4	11.8	10.4	9.3	11.4	15.4	15.5
Construction	8.0	8.1	7.6	5.7	6.3	6.4	6.5
Trade, Hotel, and Restaurant	6.9	8.1	8.4	5.6	0.6	-0.1	1.6
Transportation & Communication	18.3	17.3	15.5	15.8	16.7	17.5	16.5
Financial, Ownership & Business	8.3	8.7	8.6	7.4	6.3	5.3	5.6
Services	5.9	6.7	7.2	6.0	6.8	7.4	6.6
GDP	6.2	6.4	6.4	5.2	4.4	4.0	4.2

Source: Bank Indonesia

TRADE PERFORMANCE

Export performance has continued to fall since the Q2- 2008. This was caused by two problems: (1) plunge in commodity prices since mid-year; and, (2) weakened external demand after September 2008. Since Q1-2009, however, export showed an upward trend as the global economy geared toward a recovery. Figure 4 shows that both export value and export weight fluctuated during January 2008 – August 2009.

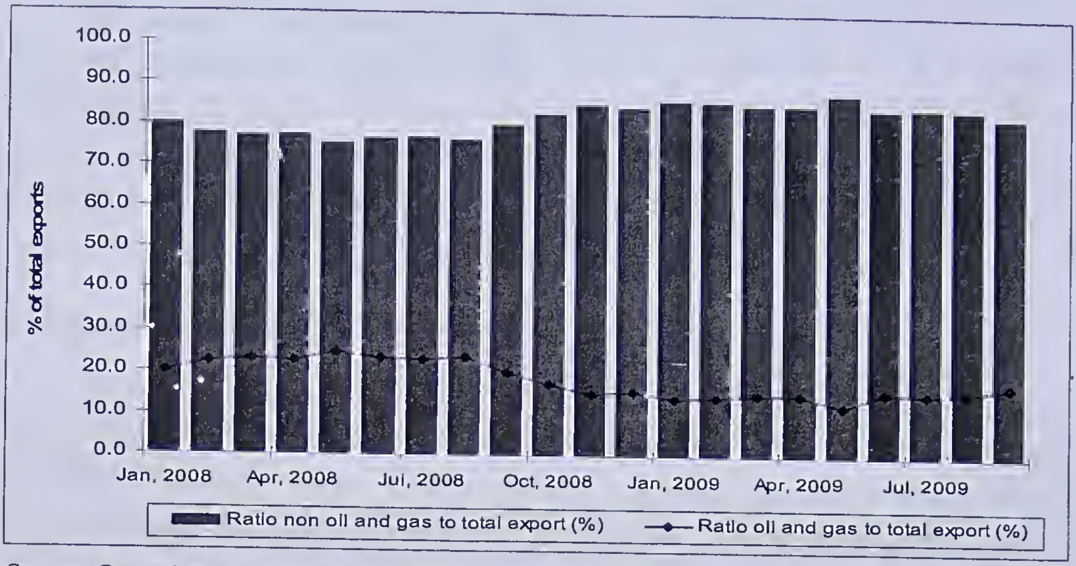
Figure 4. Indonesia's Exports, Jan 2008 - Aug 2009 (by Value and Weight)



Source: CEIC Asia Database

Non-oil and gas have always dominated exports for Indonesia. In 2008-2009, the proportion of non-oil and gas exports remained above 80%, except during Q1- 2008, owing to high prices for oil. Figure 5 shows the proportions of both oil and gas and non-oil and gas in Indonesia's total exports.

Figure 5. Proportion & Total Export of Oil and Gas Exports & Non-Oil and Gas Exports (in Percent)



Source: Central Bureau of Statistics (BPS), March 07-March 09

January 2009's year-on-year export growth dropped by 36.08%. For oil and gas exports, the decline was 57.8% on a yearly basis, with the proportion of oil and gas exports in total exports standing at 13.24%. Non-oil and gas exports, which dominated Indonesia's total exports (in January 2009, the share was 86.76%), dropped by 30.64% (year-on-year).

Out of the top 10 export commodities, animal or vegetable fats and oil (HS 15) and mineral fuels, mineral oil products (HS 27) suffered the biggest month-on-month declines in export value in September 2009, which recorded 29.2% and 8.3%, respectively. Whereas the highest increase in September 2009 was achieved at 46.9% by ores, slag and ash (HS 26).

Table 3: Non-oil and Gas Exports, Jan-Sep 2009

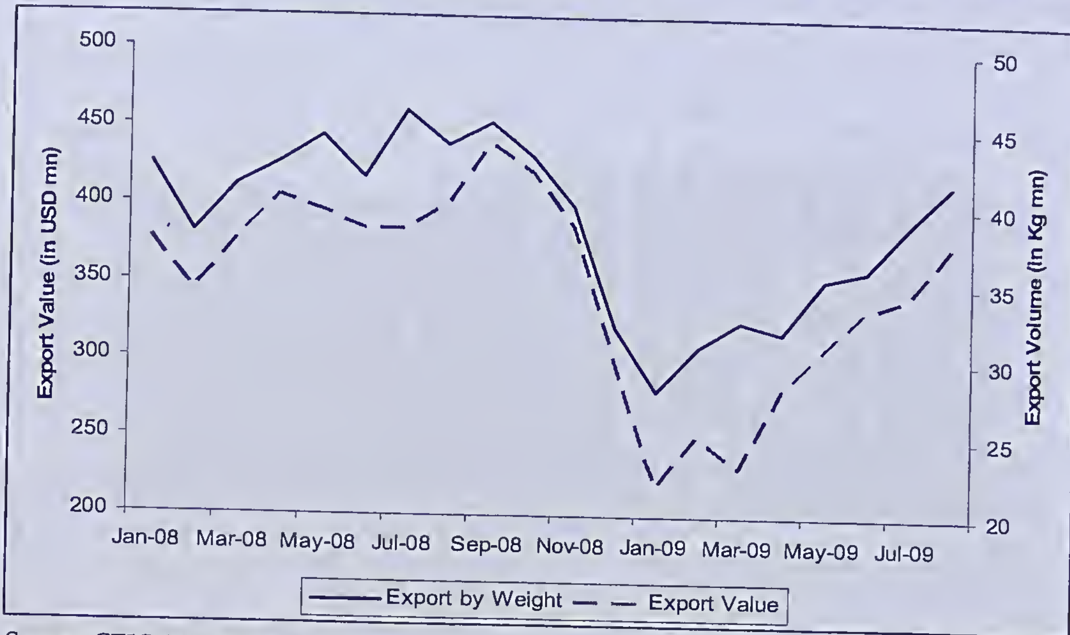
fob value (USD million)						
Commodity group (HS)	Aug-09	Sep-09	Jan-Sep 2008	Jan-Sep 2009	Change of Sept 2009 over Aug 2009 (USD million)	percent share in non-oil and gas total, Jan-Sep 2009 2009
1. Mineral fuels, mineral oil products (27)	1459.2	1337.9	7560.2	9596.9	-121.3	14.09
2. Animal or veg. fats and oil (15)	1429.9	1012.2	12268.5	8055.7	-417.7	11.83
3. Elect. Machinery, sound rec., TV etc. (85)	787.4	737.9	5939.4	5717.9	-49.5	8.39
4. Ores, slag and ash (26)	442.7	650.2	3336.2	4049.1	207.5	5.95
5. Nuclear react., boilers, mech. Appli. (84)	418.5	420.9	3762.5	3430.7	2.4	5.04
6. Rubber and articles thereof (40)	423.4	383.6	6215.3	3336.9	-39.8	4.90
7. Paper and paperboard, and articles thereof (48)	286.6	269.9	2930.9	2406.7	-16.7	3.53
8. Cooper and articles thereof (74)	212.6	238.3	1810.3	1474.2	25.7	2.16
9. Organic chemicals (29)	100.4	185.1	1508.6	1046.6	84.7	1.54
10. Ships, boats and floating struc. (89)	35.5	87.8	649.8	948.7	52.3	1.39
Total of 10 commodity groups	5596.2	5323.8	45981.7	40063.4	-272.4	58.82
Others	3294.0	2803.8	37298.4	28048.6	-490.2	41.18
Total non-oil and gas exports	8890.2	8127.6	83280.1	68112.0	-762.6	100.00

Note: * fob = free on board.

Source: Central Bureau of Statistics (BPS), November 09

Exports of electronic products (HS 85) to all destination countries in 2008-2009 showed both weight and value with a positive trend until September 2008. Then both fell down, reflecting weakening external demand. Both of its value and weight dropped to the lowest level in January 2009 by USD 219 million and 28 million kilograms, but afterwards it has continued to escalate. The biggest destination of electronic products exports has been to members of the Association of Southeast Asian Countries (ASEAN), such as Singapore and Malaysia (approximately 40% of total electronic exports). Another major destination country for electronic exports is Japan (11.81%).

Figure 6. Electronic (HS 85) Exports, 2008 (by Weight and Value)



Source: CEIC Asia Database

Diminishing demand, especially from main destination countries, has clearly taken its toll on Indonesian export performance. ASEAN is Indonesia's biggest trade partner (21.4% of total non-oil and gas export market), followed by the European Union (EU) (13.6%). For individual countries, Japan and US had the biggest share of the country's export market, accounting for 13.4% and 10.5%, respectively, in September 2009. China has become an important trade partner with a share of 8.7% in Indonesia's export market (see Table 4).

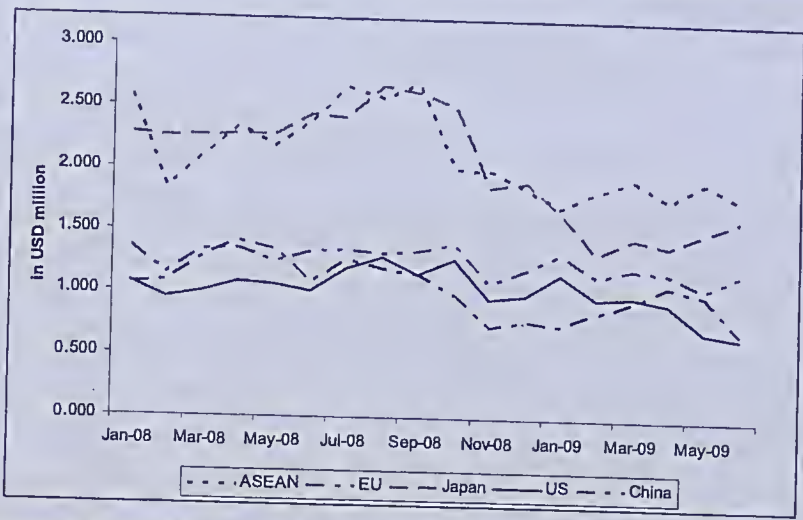
Table 4. Non-Oil and Gas Exports by Destination Country, January - September 2009

Destination	fob value (USD million)					
	Aug-09	Sep-09	Jan-Sep 2008	Jan-Sep 2009	Change of Sep 2009 over Aug 2009 (USD million)	percent share in non-oil and gas total, Jan-Sep 2009
ASEAN	1791.6	1738.3	18328.4	14440.6	-53.3	21.20
1. Singapore	662.1	685.4	7846.6	5901.9	23.3	8.66
2. Malaysia	536.8	500.3	4661.3	3789.4	-36.5	5.56
3. Thailand	251.1	233.6	2555.5	1763.5	-17.5	2.59
Other ASEAN countries	341.6	319.0	3265.0	2985.8	-22.6	4.39
Europe	1355.6	1106.9	11514.1	9671.5	-248.7	14.20
4. Germany	215.8	194.3	1891.8	1670.0	-21.5	2.45
5. France	62.0	61.5	707.8	602.8	-0.5	0.89
6. UK	130.1	100.4	1168.7	1055.6	-29.7	1.55
Other European countries	947.7	750.7	7745.8	6343.1	-197.0	9.31
Other main countries	3619.2	3449.3	33911.6	28212.3	-169.9	41.42
7. China	797.7	704.3	6477.4	5956.0	-93.4	8.74
8. Japan	1031.8	1087.7	10418.1	8091.7	55.9	11.88
9. US	941.1	850.4	9754.2	7544.7	-90.7	11.08
10. Australia	131.1	140.6	1592.2	1203.4	9.5	1.77
11. South Korea	436.3	424.7	3736.5	3378.8	-11.6	4.96
12. Taiwan	281.2	241.6	2133.2	2037.7	-39.6	2.99
Total of 12 countries	5477.1	5224.8	52743.3	42995.5	-252.3	63.12
Others	3413.1	2902.8	30536.8	25116.5	-510.3	36.88
Total non-oil and gas exports	8890.2	8127.6	83280.1	68112.0	-762.6	100.00

Source: Central Bureau of Statistics (BPS), November 09

Growth of the top 10 export products from Indonesia slowed down in January 2009. The export percentage growth to trade partners has dropped on a yearly basis, for example to ASEAN countries -41.1%, to the EU down -16%, to Japan -33%, to the US -24% and to China -33%. Particular products designated to these countries are rubber (US), palm oil (EU), coal and copper (Japan).

Figure 7. Export by Destination Country, 2008 (in USD Million)



Source: Central Bureau of Statistics (BPS), Apr 08-Mar 09.

For total non-oil and gas exports, demands among trading partners began to decrease since July 2008. Likewise, export to ASEAN countries (the biggest trading partner is Singapore) started to decline continuously beginning from July 2008. Exports to Japan have also shown a similar trend since October 2008, whereas exports to major destination countries seemed flattened towards the end of 2008.

As export performance deteriorated, import numbers began to show signs of slowdown; after surging significantly up to the third quarter of 2008, imports started to tumble. All categories of imported goods declined during January—September 2009. The biggest drop was for imports of raw materials/auxiliary goods, which declined 39%. A four percent decline in capital goods could be reflecting worsening conditions in real/manufacturing industry activities. Table 5 also shows that consumption goods imports slowed by 28.2% compared to January–September 2008.

Table 5. Imports by Economic Category, 2008-2009

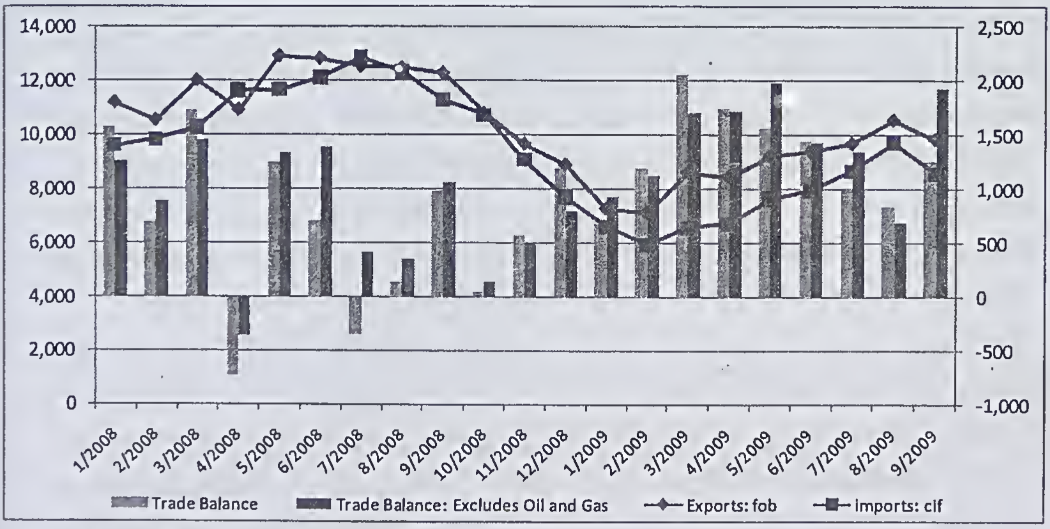
Economic category	Value (USD million) (cost, insurance and freight)		Change of Sep 2009 over Aug 2009 (%)	Value (USD million)		Change of Jan-Sep 2009* over Jan-Sep 2008 (%)	Contribution to import Jan-Sep 2009* (%)
	Aug-09	Sep-09*		Jan-Sep 2008	Jan-Sep 2009*		
Total imports	9707.3	8563.0	-11.8	101687.9	68330.9	-32.8	100.00
Consumption goods	638.5	553.7	-13.3	6706.4	4817.1	-28.2	7.05
Raw materials/ auxiliary goods	6431.8	6552.8	1.9	79626.4	48784.9	-38.7	71.39
Capital goods	2637.0	1456.5	-44.8	15355.1	14728.9	-4.1	21.56

Notes: * Preliminary figures

Source: Central Bureau of Statistics (BPS), November 09

Based on the information above, Indonesia's export and import were affected most by the global financial crisis. As can be seen on Figure 8, the rate of export and import plunged significantly during Q4-2008 until Q1-2009., and reached its lowest value in February 2009. Nevertheless, it started to climb up slowly in Q2 and Q3- 2009.

Figure 8. Indonesia's Trade Performance, January 2008-September 2009 (in USD Million)



Source: Central Bureau of Statistics (BPS)

CONCLUSION

In response to deteriorating conditions in the global economy, Indonesian government has taken both reactive and proactive measures. The government and the central bank have made cooperative efforts to maintain financial market stability and to provide a fiscal stimulus in order to keep domestic demand growth at its usual annual rate. So far, the Indonesian economy has managed to be the country in the Asian region that has had positive growth predictions this year (2009). Asian economies rebounded in Q2-2009 as aggressive monetary and fiscal stimuli cushioned domestic demand and quick inventory adjustment eased the downturn in industrial production. Capital inflows have buoyed the asset markets and net exports have contributed to GDP growth as imports have contracted faster than exports. However, policy measures are inadequate to close the output gap emanating from sluggish private demand and sharp export contraction. Regarding to that condition, Asian economies, especially Indonesia, has experienced slow positive growth in 2009.

Developments in the global financial crisis have clouded Indonesia's economic outlook. Factors, such as drops in commodity prices, slower global growth, and tighter liquidity in financial markets across emerging economies have dragged down exports and investments. In fact, the latter are keys to Indonesia's economic growth. So far, the impacts of the current global crisis have been severe to externally oriented sectors, such as manufacturing industry, with the number of layoffs increasing since October-November 2008. Rupiah's depreciation and capital outflows volatility have put more pressures on the domestic economy. However, the positive signal started to take place after the general election where Rupiah has begun to experience appreciation and the capital/stock market, IDX, has showed the bullish trend.

Having learned from the previous crisis (1997-1998), Indonesia's government was quick to respond by combining both monetary and fiscal policy instruments in order to at least minimize global crisis impacts on Indonesia's election year of 2009. Swift action in the handling of the rapid depreciation of the Rupiah since August 2008 had helped the government successfully manage to avoid the sudden meltdown of 1998.

As the crisis is expected to worsen in developed countries, export and investment growth will be stagnant accordingly. Growth will be adversely affected. However, efforts to bring down unemployment and poverty should continue and these are very much influenced by the level of economic growth. Indonesia has now become dependent much more than before on its own spending as an engine of growth. Having assessed the situation, the government has prepared a stimulus package consisting of two parts: (1) the tax saving programme, which will go directly to households and businesses; and, (2) additional spending on infrastructure projects that are expected to create big multiplier effects in household and private sector spending.

In addition, there are some factors that may keep household spending up and in turn support the effectiveness of the fiscal stimulus package, namely, low commodity prices on the international market owing to falling demand, good seasonal weather and the fact that 2009 was Indonesia's election year, where electoral (both legislative and presidential) candidates spent money on their campaigns. However, countries with huge domestic demands, attractive asset markets, greater policy space, and faster reforms—such as, China and Indonesia—may prove themselves to be resilient in facing the global financial crisis.

INDONESIA'S CHANGING STRATEGIC LANDSCAPE: RECENT TRENDS AND FUTURE CHALLENGES

Evan A. Laksmana

In recent months, developments in Indonesia's geostrategic landscape, especially in the Asia Pacific region, seem to follow existing trends in the past few years. The main trends in this regard are the continued rise in overall defence spending, the growing sophistication of naval and air force, and the growing self-reliance of regional defence industries.

These trends seem set to continue for the foreseeable future as many of the development plans outlined by regional militaries are within a ten to twenty year time frame. Indonesia needs to take note of these developments and prepare measures to either keep up, or risk being strategically irrelevant.

"FOLLOW THE MONEY": THE CLIMBING REGIONAL DEFENSE SPENDING

Despite a brief lull period due to the economic crisis of the 1990s, defence spending and modernization in the Asia Pacific region has continued to climb. By 2004, according to *SIPRI*, East Asian states continue to spend more on weapons than any other region in the developing world. In fact, defence spending throughout Northeast Asia has

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returned to pre-1997 levels and has increased by over 19% since 11 September 2001.

Even by conservative estimates, China's defence budget has more than doubled since 1997 and more than tripled since 1989. Between 2001 and 2005, it rose by an estimated 57%. However, in 2009 the rate of defence budget increase has been lowered to 14.9% from 16.5% in 2008.

Increasingly concerned by North Korea's unpredictable behaviour, and by China's military build-up, Japan is taking steps to review and enhance its existing defence posture. Although defence spending might decrease by 3% over the next five years due to domestic economic constraints, Japan is compensating troop reductions and cuts to conventional systems by developing new capabilities, including new rapid-reaction forces, a ballistic missile shield, and the improvement of satellite communications and intelligence gathering.

In India, the Mumbai terrorist attacks of November 2008 led to an interim budget in which defence spending was increased by 34% in 2009, much of which was spent on personnel. The official budget announced in July maintained the USD37.75 billion budget announced in the interim budget. Further increases in defence spending are expected as border security issues with Pakistan continue and the threat of terrorist attacks remains.

Plans to withdraw up to one-third of American forces and to redeploy the remainder away from the demilitarized zone (DMZ) are accelerating South Korea's drive for 'independent defence' since 2004. Its defence budget increased by an average of 4.5% per year from 2002 to 2005, and its overall combat capability is being significantly upgraded as part of a USD178 billion Defence Reform 2020. This includes an allocation for 267 arms build-up projects to beef up its surveillance and precision strike capability. The new Australian government's first budget included a 6.4 percent spike in the 2008–09 defence expenditure and a commitment that spending would continue to rise by 3% in real terms until 2017.

In Southeast Asia, according to *Jane's Defence Weekly*, official defence spending climbed at an average annual rate of 13.5% in three years before the economic downturn in 2008—but in 2009, the growth continues at 6% to around USD26 billion and it is projected to grow by 8 to 9% annually until 2012.

Malaysia's spending increased by 19% between 2001 and 2005, and has almost doubled since 1998. Meanwhile, in 2005 Singapore's defence budget also increased by 7% from the previous year. The budget in 2008 and 2009 was also steady at around USD7 billion. Even the tiny Cambodian government has proposed to raise its defence budget for next year to USD274 million, an increase of nearly 23% from 2009. According to *Jane's Defence Weekly*, this would amount to around 14% of Cambodia's total spending for FY10. According to The Military Balance, the Philippines has also increased its defence budget more than 20% to PHP56.5 billion in 2008, with a further 9.6% spike in 2009, said *The Military Balance*.

In Thailand, the defence budget continues to climb after Thaksin Shinawatra's governments (2001–06) kept defence spending down. In 2007, the budget jumped by 20%, and in 2008, it was increased by a further 25% to USD4.2 billion. The budget for fiscal year 2009 was THB169.1 billion. Recently, the *Asian Defence Journal* reports that the Thai cabinet approved about THB10 billion (USD 320 million) tied-over budget for military procurement spread to 2012, including military ordnance, anti-submarine warfare capabilities, and coastal patrol boats.

"COME THE REVOLUTION": THE GROWING SOPHISTICATION OF NAVAL AND AIR POWER

Along with the rise in defence spending, the high-tech IT-driven 'Revolution in Military Affairs' have also led to the growing sophistication of regional armed forces, especially in terms of air and naval power. More importantly, available resources are being directed toward externally oriented weapons systems such as fighter aircraft, surface ships, submarines, and missiles.

In terms of air power, between 1997 and 2004, scholars note that over 900 supersonic combat aircrafts were acquired in Asia, along with some 9,500 surface-to-air (SAM), surface-to-surface (SSM), and anti-ship missiles (ASM).

In Australia, the Defence Materiel Organization, BAE Systems Australia, and Australian Aerospace signed a contract in late July to provide a range of enhancements to the AP-3C Orion Aircraft fleet and associated ground support systems for the Air Force (*Asian Military*

Review). Furthermore, the first of their new 24 F/A-18F Super Hornet was unveiled in early July and is expected to arrive next year.

Meanwhile, *Asian Defence Journal* reports that South Korea intends to purchase an additional 21 units of Boeing F-15K fighters under an overall F-X or next-generation fighter programme. To support these new fighters are: 150 KF-16s, which could carry the advanced precision-guided Joint Direct Attack Munitions (JDAM) missiles by the end of the year, its first Airborne Warning and Control Platform E-737 by 2011, and more than 20 semi-indigenous T-50 Golden Eagle supersonic jet trainers.

Singapore, as reported by *The Military Balance*, might see later this year the first batch of its F-15SG combat aircraft, out of 24 ordered so far, along with the Gulfstream G550 Conformal Airborne Early Warning Aircraft. Thailand have also negotiated to obtain the *Gripen* multi-role combat aircraft, Saab 100 *Erieye* airborne early-warning aircraft as well as a new air-defence system, according to *The Military Balance*. The Philippines is also attempting to upgrade its Air Force as part of the Capability Upgrade Program (CUP) for the armed forces. Malaysia also plans to buy additional combat aircraft (either additional Su-30-MKKs or F-18E/Fs) and airborne early-warning aircraft.

There also appears to be a growing trend of moving into acquiring Unmanned Aerial Vehicles (UAVs). In South Korea, the state-funded Agency for Defence Development plans to produce an indigenous guided bomb to be carried by a UAV, as reported by *Asian Defence Journal*. According to The Military Balance, Singapore is also known to be interested in the RQ-4 *Global Hawk* UAV for maritime reconnaissance, but no decision has been made.

On the naval side, global spending on new construction of naval platforms over the next 20 years would total around USD640 billion, according to the AMI International, a naval consultancy agency. The Asia-Pacific region would account for a large share of the pie here. China, Japan, and South Korea are forecasted to spend some USD60 billion over the next five years on strengthening their fleets. This figure is projected to reach USD108 billion over the next decade and USD173 billion over the period to 2030.

Earlier in August, *Asian Military Review* reported that Australia plans to comprehensively upgrade its Anzac frigate fleet (for about

ASD158 million) as part of the anti-ship missile defence (ASMD) programme set out in a recently released Defence White Paper. Moreover, according to *Jane's Defence Weekly*, Australia's submarine fleet will double in size from six to 12 boats and a new class of 20 multirole offshore combatant vessels will take up patrol, hydrographic and mine countermeasures duties. Six heavy landing craft and a new replenishment and logistic support ship will also be purchased and a fleet of at least 24 new naval combat helicopters will join six MRH 90 utility helicopters already on order.

Meanwhile, according to *India Defence*, India plans to add new major surface vessels, including six indigenous *Kolkata* class stealth destroyers, six Russian *Talwar* class frigates, and the vertically launched Russian *Klub* ASCM, along with twelve indigenous *Shivalik* tealth frigates. Similarly in Malaysia, *The Military Balance* reported that it has signed a letter of intent for two British-built *Jebat*-class frigates, which are intended to enter service by 2015, and in the longer term, the navy intends to acquire three LPD-type multi-role support ships, Hydrographic Ships, and upgrade its Naval Electronic Warfare Support Systems.

The growth of sub-surface warfare capabilities has also become prevalent in the Asia Pacific region. Eight navies in the region had submarines in the mid-1980s and that figure has since grown to twelve. *Jane's Defence Weekly* predicted that the regional Anti-Submarine Warfare market could be worth up to USD7.4 billion in 2015. In fact, some reports suggest that around 80 to 100 new submarines will be procured for the navies of India, Pakistan, China, Taiwan, Japan, South Korea, Vietnam, Malaysia, Singapore, and Indonesia by 2018. Most will be modern conventional submarines equipped with advanced technologies.

China's naval expansion is also said to include plans to operate about 50 current-generation submarines by 2010-2012, including three to six new second-generation nuclear-powered submarines, and two or three Type 094s. In addition, perhaps three new bases are being constructed that are expected to be devoted to new submarines. In response, Japan announced its plans to acquire anti-submarine capabilities. Under current funding allocations, it has the resources to procure one destroyer and one submarine each year.

Similarly, India has launched on 26 July 2009 its first indigenously built nuclear submarine, INS *Arihant*, and is license-producing six *Scorpène* submarines and plans to build three to five additional ballistic missile submarines by 2015-2017. This falls within its plan to develop a blue water naval capability by 2022. The long term goal is to construct a total of twenty-four submarines over fifteen to twenty years. Singapore has taken delivery of four Swedish-manufactured *Sjoormen*-class diesel submarines, and plans to order more in the future, according to *Jane's Information Group*. In September this year, Malaysia has also received their first *Scorpene*-class submarine KD Tunku Abdul Rahman from France.

Additionally, regional militaries are increasingly focused on the modernization and sophistication of their Command, Control, Communications, Computers (C4I) and Intelligence, Surveillance, and Reconnaissance (ISR) system. According to *Jane's Defence Weekly*, Singapore recently established an agency to address cyber threats and national IT security issues called the Singapore Infocomm Technology Security Authority (SITSA)—which became operational starting from 1 October. Malaysia, as part of its "Fourth Dimension Malaysian Armed Forces" (4D-MAF) focusing on joint force and information superiority, also plans to purchase an Airborne Early Warning and Control, which has been approved recently during the 9th Malaysia plan—though it seems to be on hold. This nevertheless signifies the shift in emphasis by the MAF away from procurement of traditional platform-centric equipment toward information technology and network-based systems.

"ON OUR OWN FEET": THE GROWING SELF-RELIANCE OF REGIONAL DEFENCE INDUSTRIES

Given the increasingly complex and fluidly changing regional balance of power, many of the Asian countries' domestic defence industries are moving, or trying to move, to a more self-reliant and independent posture. Military analysts, Richard Bitzinger and Kenneth Boutin, have recently argued that China's defence-industrial sector is being transformed by reforms, becoming more decentralized, and the contributions of local state-owned enterprises (SOEs) and privately-owned companies are increasingly more critical, especially in research and development (R&D).

Simultaneously, Beijing has been prodding defence industries to undertake more civilian production as a means of acquiring dual-use technologies, including microelectronics, space systems, new materials, propulsion, missiles, computer aided manufacturing and IT. Offset policies also became China's key focus to reach defence self-sufficiency. For example, driven directly by Beijing, the space and aviation sector is targeting the indigenous development of a large-scale jet airliner (of the scale of a Boeing 747 or the Airbus A380) by 2020.

Australia is also updating its defense industry policy, scheduled to be published by the end of this year. According to *Jane's Defence Weekly*, the new policy will be shaped by three key themes: (1) a sectoral approach to industrial development; (2) a focus on global supply chains; and, (3) a "new approach" to defence procurement. said. The new policy also envisaged an "empowered" Defence Material Organization. Meanwhile, in Malaysia, scholars have argued that its defence industry development was mainly aimed at self-reliance in spares and logistic support, modification, upgrades, retrofits, maintenance, repair and overhauls without foreign assistance. Recently, Malaysia proposed to establish an ASEAN Security and Defence Industry Council (ASDIC), which was approved by the group's defence ministers in November and is expected to be formed before a regional meeting in May 2010.

As reported by *Jane's Defence Weekly*, Thailand has also decided in early November to increase indigenous defence manufacturing targets in response to the growing costs of military procurement—and eventually reverse the current ratio whereby Thai state-owned industries produce just 10% of nationally procured equipment. Offset policies and technology transfer is also part of this strategy, including the purchase of the JAS-39 *Gripen* multi-role combat aircraft, where Gripen agreed to transfer 100 "man-years" of technologies to Thailand, train nearly 100 Royal Thai Air Force engineers and transfer source codes and software to Thai industries. Additionally, Thailand's MoD is seeking to increase self-reliance through subsidizing industries' development and production of items as well as through the creation in January of the MoD's Defence Technology Institute.

FUTURE CHALLENGES FOR INDONESIA: STEP UP OR STEP OUT

These regional developments clearly show that Indonesia is way behind in terms of force development. Investments in R&D, as well as

innovative procurement strategies geared to strengthen domestic defence industry with a long term vision of self-sufficiency, have all stood behind the growing sophistication of regional militaries. Indonesia's key neighbours, especially Malaysia and Singapore, have also increased their naval and air power projection capabilities significantly—which further widens the regional gap between the three countries.

Furthermore, the growing sophistication of network-centric systems in those countries when coupled with its increasing surveillance and patrol capabilities could make it harder for Indonesia to monitor and defend its territorial waters, especially in terms of response time. Developments in Northeast Asia also signal an emerging naval rivalry which could destabilize the region and threaten Indonesia's northern zone of defence and Sea Lines of Communications (SLOCs).

Therefore, unless Indonesia wants to be strategically irrelevant in the region, the Indonesian government should consider the following. First, it needs to create a Defence Policy Board consisting of both experts and policymakers to outline a comprehensive long-term defence plan. Such planning must tackle issues relating defence self-reliance, personnel policies and military education, as well as a realistic assessment of Indonesia's regional strategic environment.

Second, given the growing sophistication of naval and air power, Indonesia would not predictably do well in preparing for any related contingencies by expanding the number of troops or expanding the territorial command as recently announced. If anything, Indonesia should necessarily go against the current regional trend that is replacing mass with technology.

Third, Indonesia needs to redefine its "Minimum Essential Force" to move away from a platform-centric development to a network-centric development by focusing on high-tech hardware, highly-educated brainware, and well-developed software. This could also further boost the military's stated goal of joint operations.

Finally, the President should immediately establish a National Security Council to help oversee the process. The day-to-day activity of this council should differ from the current activities of the Coordinating Ministry for Political and Security Affairs. One should not forget that in a changing regional environment, adaptation and innovation are the prime virtues for survival.

Vol. 38, No. 2
Juni 2009

ISSN 1829-5908

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